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APPENDIX

In the

Supreme Court of the United States

OCTOBER TERM, 1974

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No. 1042

ERNST & ERNST, *Petitioner,*

vs.

OLGA HOCHFELDER, ET AL., *Respondents.*

ERNST & ERNST, *Petitioner,*

vs.

LEON S. MARTIN, ET AL., *Respondents.*

On Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

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Petition For Certiorari Filed February 20, 1975
Certiorari Granted April 14, 1975

IN THE
SUPREME COURT OF THE UNITED STATES
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* As the First Amended Complaint of Plaintiffs Martin et al. is essentially identical, it is not reproduced in this Appendix.

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APPENDIX

CHRONOLOGICAL LIST OF RELEVANT DOCKET ENTRIES

February 19, 1971—Plaintiffs Hochfelder et al. filed original complaint in U.S. District Court for the Northern District of Illinois (71 C 454).

April 19, 1971—Defendant Midwest Stock Exchange filed motion for summary judgment in 71 C 454.

May 18, 1971—Plaintiffs Martin et al. filed Original Complaint in U.S. District Court for the Northern District of Illinois (71 C 1204).

September 3, 1971—Order entered by stipulation that ruling in 71 C 454 will control ruling in 71 C 1204 on motion for summary judgment of defendant Midwest Stock Exchange.

October 21, 1971—Plaintiffs Hochfelder et al. and Plaintiffs Martin et al. filed essentially identical first amended complaints in 71 C 454 and 71 C 1204, respectively.

November 29, 1971—Defendant Midwest Stock Exchange filed essentially identical answers to the first amended complaints of Plaintiffs Hochfelder et al. and Plaintiffs Martin et al. in 71 C 454 and 71 C 1204, respectively.

March 13, 1972—Defendant Midwest Stock Exchange filed essentially identical motions for summary judgment in 71 C 454 and 71 C 1204.

August 24, 1972—Defendant Ernst & Ernst filed answer to first amended complaint of plaintiffs Hochfelder et al. in 71 C 454.

October 3, 1972—Decision and order entered granting summary judgment for defendant Midwest Stock Exchange in 71 C 454.

October 20, 1972—Final judgment entered in favor of defendant Midwest Stock Exchange in 71 C 454.

October 20, 1972—Order entered that summary judgment be granted for defendant Midwest Stock Exchange in 71 C 1204 for the same reasons set forth in the order of October 3, 1972 in 71 C 454.

November 2, 1972—Plaintiffs Hochfelder et al. and Plaintiffs Martin et al. filed notice of appeal of order granting summary judgment for defendant Midwest Stock Exchange in 71 C 454 and 71 C 1204, respectively.

November 6, 1972—Defendant Ernst & Ernst filed answer to first amended complaint of plaintiffs Martin et al.

December 11, 1972—Defendant Ernst & Ernst filed identical motions for summary judgment in 71 C 454 and 71 C 1204.

August 1, 1973—Decision and order entered granting summary judgment for defendant Ernst & Ernst in 71 C 454 and 71 C 1204.

August 31, 1973—Plaintiffs Hochfelder et al. and Martin et al. filed notice of appeal of order granting summary judgment for defendant Ernst & Ernst in 71 C 454 and 71 C 1204, respectively.

November 25, 1974—Certified copy of an order of the United States Court of Appeals for the Seventh Circuit filed affirming summary judgment for defendant Midwest Stock Exchange and of the United States Supreme Court denying a writ of certiorari in 71 C 454 and 71 C 1204.

January 30, 1975—Certified copy of an order of the United States Court of Appeals for the Seventh Circuit filed reversing summary judgment for defendant Ernst & Ernst and denying rehearing in 71 C 454 and 71 C 1204.

April 17, 1975—Order entered staying all proceedings in 71 C 454 and 71 C 1204 pending ruling by United States Supreme Court on writ of certiorari.

IN THE UNITED STATES DISTRICT COURT

• • (Caption — No. 71 C 454) • •

FIRST AMENDED COMPLAINT

(October 21, 1971)

FIRST COUNT

1. The defendant, Midwest Stock Exchange, is an unincorporated association registered as a National Securities Exchange under Section 6 of the Securities Exchange Act of 1934 as amended, 15 U.S.C. §78f.

2. This action is brought under Section 10 of the Securities Exchange Act of 1934 as amended, 15 U.S.C., §78j. This Court has jurisdiction thereof under Section 27 of the Securities Exchange Act of 1934 as amended, 15 U.S.C., §78aa.

3. Plaintiffs prior to June 1, 1968 were securities customers of First Securities Company of Chicago, a securities dealer with offices on LaSalle Street in Chicago, the President of which, and the owner of 92% of the stock of which, was Leston B. Nay, a member of the defendant, Midwest Stock Exchange.

4. Nay fraudulently persuaded each of the plaintiffs to sell his securities through First Securities Company of Chicago and fraudulently persuaded each of them to invest the proceeds, aggregating $972,500 for all plaintiffs in a fictitious and non-existent escrow and issued to each of them a security therefor on the letterhead of First Securities Company, "member Midwest Stock Exchange". Nay converted such proceeds to his own use immediately on their receipt. In so defrauding each of the plaintiff customers, Nay used the mails, the public telephone system and the facilities of a National Securities Exchange. Nay shot and killed himself in June, 1968, his estate has

no assets, and First Securities Company of Chicago is insolvent.

5. Nay's said fraud violated Section 10 b of the Securities Exchange Act of 1934 and Rule 10 B-5 of the Securities Exchange Commission promulgated under the authority of said Section 10 of the Securities Exchange Act of 1934 (15 U.S.C., Section 78j).

6. Under the terms of Section 6 of the Securities Exchange Act of 1934, Midwest Stock Exchange was required to file and did file with the Securities and Exchange Commission as a condition of its registration an agreement to "enforce so far as is within its powers compliance by its members with the provisions of this title, and any amendment thereto and any rule or regulation made or to be made thereunder".

7. Rule 10 b-5, 17 Code of Federal Regulations, Section 240.10 b-5, 1968, promulgated by the Securities Exchange Commission under Section 10 of the Securities Exchange Act of 1934 provided as follows:

> "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud.
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

> in connection with the purchase or sale of any security."

8. The defendant, Midwest Stock Exchange, aided and abetted Nay in his violation of the Act and Rule aforesaid, among others, in the following ways:

(a) The Exchange represented to the public, including plaintiffs, that members of the Exchange were persons of honor and integrity, who were worthy of confidence and trust. It issued Nay a certificate in large, bold type for permanent posting on the wall of Nay's office held the customers of Nay customers and the public that Leston B. Nay of First Securities Company of Chicago was a member of Midwest Stock Exchange "Where High Standards Of Commercial Honor And Integrity Are Maintained". Nay's membership in the Midwest Stock Exchange and the aforesaid certificates so posted on the wall of Nay's office had the customers of Nay and First Securities Company, including plaintiffs, to believe that Midwest Stock Exchange had diligently investigated Nay before accepting him for membership and had continued thereafter to make adequate investigations to assure itself that Nay was in fact maintaining high standards of commercial honor and integrity. Said certificate was used and exhibited by Nay in defrauding plaintiffs as aforesaid and plaintiffs relied upon it. Defendant made no proper investigation before admitting Nay to membership and before issuing the said certificate to Nay; it failed to secure any commercial report regarding him; failed to make any inquiry of his prior employer for twelve years; failed to discover that he had changed his name; and failed to make any investigation of the two suits in which he had been

twice divorced from his wives. Midwest Stock Exchange did not thereafter sufficiently investigate Nay and First Securities Company to make certain that high standards of commercial honor and integrity were maintained by him or it. Had the Exchange done so, it would have discovered that Nay was not a man of honor and integrity when it accepted him for membership and issued him the certificate and that he was not a man of honor and integrity thereafter.

(b) For several years before Nay's suicide, the Exchange had knowledge of his extraordinary large and continuous borrowings from First Securities Company ultimately aggregating some $84,000. The Exchange then knew that First Securities Company was in a perilous financial condition and should have investigated it and any such investigation would have disclosed that Nay was wholly unable to pay his said indebtedness. He had liabilities of more than $1,000,000 and only nominal assets and was wholly insolvent. Such investigation would have disclosed Nay's fraud toward the plaintiffs herein. When the auditors for the Exchange reported to the Exchange in 1967 that in view of Nay's borrowings from First Securities Company its capital was less than the minimum capital of $25,000 required by the Exchange, it permitted Nay temporarily to pay $10,000 on his indebtedness to First Securities, thus for a few weeks restoring its capital to the minimum requirements and the Exchange instructed its auditors not to note on their report that the Company's capital had been reduced below such minimum requirements.

(c) Nay kept a private record of the aforesaid fictitious escrow investments locked in his desk at

First Securities Company and no record of them appeared on the books of First Securities Company. He took no vacations and on his emphatic instructions no mail addressed to him or to First Securities Company for his attention was opened by anyone but him. He was thus able to keep secret from the officers and directors of First Securities Company the considerable correspondence that he had with the plaintiffs in perpetrating said fraud, much of which was on the letterheads of First Securities Company "Member Midwest Stock Exchange". This procedure violated Rule 27(c) of the National Association of Securities Dealers, a body organized under statutory authority to perform under oversight of the Securities and Exchange Commission, regulatory functions, and a body of which Nay and First Securities Company were members, which rule provides as follows:

> "(c) Each member shall be responsible for keeping and preserving appropriate records for carrying out the member's supervisory procedures. Each member shall review and endorse in writing, on an internal record all transactions and all correspondence of its registered representatives pertaining to the solicitation or execution of any securities transaction."

The above rule was approved by the Securities and Exchange Commission and constitutes the standard of the securities industry compliance with which by its members the Midwest Stock Exchange was obligated to enforce. The purpose of this Rule was to prevent such fraud as was perpetrated in this case by an officer of a securities dealer having securities transactions known only to him. It was within the

power, and was the duty, of the defendant, Midwest Stock Exchange as a registered National Securities Exchange for the protection of the customers of its members to enforce compliance by its members with the procedures required by the above rule. Enforcement of this rule was further a duty of the Exchange in light of its continuing representation to the public, including plaintiffs, that members of the Midwest Stock Exchange were persons who maintained high standards of commercial honor and integrity. It failed to enforce compliance with the said rule by its member, Leston B. Nay, and First Securities Company, and the losses of the plaintiffs as aforesaid were the result of the said failure of the said defendant to enforce compliance with said rule.

(d) As a condition of its registration as a National Securities Exchange by the Securities and Exchange Commission, the defendant, Midwest Stock Exchange, adopted the following Rule as Article XX, Rule 4 and the said Rule was approved by the Securities and Exchange Commission:

> "A surprise audit of the affairs of each such member, member firm and member corporation shall be conducted annually by independent public accountants at a date to be selected by such accountants and approved by the Exchange, but without prior notice to such member, member firm or member corporation. On or before January 10 of each year each such member, member firm and member corporation shall notify the Exchange of the name of the independent public accountants appointed for such year and, unless the Exchange disapproves of such appointment, such accountants shall conduct such surprise annual audit and prepare and file wtih the Exchange an answer to the Exchange financial questionnaire based upon such audit."

It was the duty of the defendant, Midwest Stock Exchange as a National Securities Exchange by its financial questionnaire as aforesaid, or otherwise, to require the independent public accountants mentioned in the foregoing Rule to report and certify the methods of internal accounting control of its members and particularly whether or not its member had complied with the procedures set out in the aforesaid Rule 27 (c) of the National Association of Securities Dealers. The financial questionnaire of the Midwest Stock Exchange as aforesaid made inquiry of the said independent public accountants on the methods of internal accounting control of Nay and First Securities Company, but the said independent public accountants failed to answer properly or adequately the said questionnaire with respect to such internal accounting control and the Midwest Stock Exchange failed to require such answers, thereby permitting Nay and First Securities Company to defraud the plaintiffs as aforesaid.

(e) Midwest Stock Exchange, in pursuance of its obligations as a registered National Securities Exchange, was obligated to enforce, so far as was within its power, compliance by its members with the provisions of the Securities Exchange Act of 1934 and all regulations made thereunder, and it was within the power of Midwest Stock Exchange to ascertain whether or not Nay or First Securities Company of Chicago had any financial commitments that were not contained in the ledger accounts of First Securities Company. Midwest Stock Exchange

failed to require its member, Leston B. Nay, and its member, First Securities Company, to disclose such financial commitments, whereby plaintiffs were defrauded as aforesaid.

9. By such failures as aforesaid the defendant, Midwest Stock Exchange, aided and abetted the aforesaid violation by Nay of Section 10 of the Securities Exchange Act of 1934 and Rule 10 b-5 of the Securities Exchange Commission.

10. Plaintiffs have been required to employ attorneys to present this claim and prosecute this action. Plaintiffs are entitled to recover for the reasonable services of such attorneys.

Wherefore, plaintiffs demand judgment against the defendant, Midwest Stock Exchange, for Nine Hundred Seventy Two Thousand Five Hundred ($972,500) Dollars; for a reasonable fee for plaintiffs' attorneys; for the costs of this action; and for all other relief as may be just and proper in the premises.

SECOND COUNT

1. At all times hereinafter mentioned the defendant, Ernst & Ernst, was a partnership with an office in Chicago, Illinois, engaged in the profession of Certified Public Accounting under the Illinois statutes and so held itself out to the public.

2. Plaintiffs bring this action under §10 of the Securities Exchange Act of 1934 as amended, 15 U.S.C. §78 j. This Court has jurisdiction thereof under §27 of the Securities Exchange Act of 1934, as amended, 15 U.S.C. §78 aa.

3. Plaintiffs prior to June 1, 1968 were securities customers of First Securities Company of Chicago, a securities dealer with offices on LaSalle Street in Chicago.

the President of which, and the owner of 92% of the stock of which, was Leston B. Nay, a member of the Midwest Stock Exchange.

4. Nay fraudulently persuaded each of the plaintiffs to sell his securities through First Securities Company of Chicago and fraudulently persuaded each of them to invest the proceeds, aggregating $972,500 as to all plaintiffs, in a fictitious and non-existent escrow and issued to each of them a security for said investment on the letterhead of First Securities Company, Member Midwest Stock Exchange. Nay converted their said money to his own use immediately upon its receipt. In so defrauding each of the plaintiffs, Nay used the mails, the public telephone system and the facilities of National Securities Exchanges. Nay shot and killed himself in June, 1968. His estate has no assets and First Securities Company of Chicago is insolvent.

Nay's said fraud violated Section 10 b of the Securities Exchange Act of 1934 and Rule 10 b-5 of the Securities Exchange Commission promulgated under the authority of said Section 10 of the Securities Exchange Act of 1934, 15 U.S.C. Section 78 j.

5. Rule 10 b-5 aforesaid, 17 Code of Federal Regulations, §240.10 b 5, 1968, promulgated by the Securities Exchange Commission under Section 10 of the Securities Exchange Act of 1934 provides as follows:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud.

(b) To make any untrue statement of a material fact or to omit to state a material fact

necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security."

6. The defendant, Ernst & Ernst, aided and abetted Nay in his violation of the Rule and Act aforesaid, among others, in the following ways:

(a) For several years prior to June 1, 1968, Ernst & Ernst, as Certified Public Accountants, were employed by Nay and First Securities Company to furnish to the Midwest Stock Exchange an annual surpise audit of First Securities Company as required by the rules of the Midwest Stock Exchange. Ernst & Ernst, as Certified Public Accountants, knew, or should have known, that the purpose of said audit was to enable the Midwest Stock Exchange to continue to represent to the public that Nay, as a member of the Midwest Stock Exchange, was a person with a high standard of commercial honor and integrity and that the purpose of such audit report was, therefore, to protect customers of Nay and First Securities Company against loss by fraud.

(b) Ernst & Ernst knew, or should have known, that investors in dealing with Nay and First Securities Company would rely on Nay's membership in the Midwest Stock Exchange, as the plaintiffs did rely, and that the continuance of said membership was dependent on the accuracy and completeness of the surprise audit report by Ernst & Ernst to the Midwest Stock Exchange.

(c) Ernst & Ernst failed to exercise proper or appropriate auditing procedures in making said audit of First Securities Company among others in the following respects:

(i) Under standard auditing practice it was the duty of Ernst & Ernst as such auditors to make adequate and proper inquiry on whether the officers and employees of First Securities Company took regular vacations, and whether during such vacations their duties were performed by other employees; and Ernst & Ernst failed to make such inquiry and failed to discover that Nay, the president of the company, took no regular vacations; and that the mail addressed to the Company piled up unopened on his desk when, for a single day or more, he was absent from the office, and thus Ernst & Ernst failed to discover that First Securities had no adequate or proper accounting control.

(ii) Under standard auditing practice it was the duty of Ernst & Ernst as such auditors to make adequate and proper inquiry on the standard rules of First Securities Company regarding the opening of mail, and Ernst & Ernst failed to make such inquiry and failed to discover that Nay as president of the company required that all mail addressed to the Company for his attention be opened only by him and thus failed to discover that the company had no adequate or proper accounting control.

(iii) Ernst & Ernst knew, or should have known, that Nay took no regular vacations and forbade the officers and employees of First Securities Company to open any mail addressed

to him or to First Securities Company for his attention and that he thus kept secret from the other officers of First Securities Company the considerable correspondence that he had with the plaintiffs in perpetrating said fraud, much of which was on the letterheads of First Securities Company, "member Midwest Stock Exchange". This procedure violated Rule 27 (c) of the National Association of Securities Dealers, a body organized under statutory authority to perform, under oversight of the Securities and Exchange Commission, regulatory functions, which provided as follows:

> "(c) Each member shall be responsible for keeping and preserving appropriate records for carrying out the member's supervisory procedures. Each member shall review and endorse in writing, on an internal record, all transactions, and all correspondence of its registered representatives pertaining to the solicitation or execution of any securities transaction."

Despite the fact that Nay and First Securities Company were members of said National Association of Securities Dealers and that the procedure required by the foregoing rule constitutes the standard of the securities industry, no effort whatever was made by Nay or First Securities Company to comply with the foregoing rule and it was the duty of Ernst & Ernst as Certified Public Accountants to report said failure to the Midwest Stock Exchange, and Ernst & Ernst as such auditors failed to report in its said audit reports to the Midwest Stock Exchange such non-compliance with said rule, thus omitting to state a material fact in its said audit reports, and the

losses of the plaintiffs as aforesaid resulted from such failure.

7. Under the terms of the employment of Ernst & Ernst as Certified Public Accountants to make such audit, it was the duty of Ernst & Ernst to prepare and file with the Midwest Stock Exchange an answer to the Midwest Stock Exchange's financal questionnaire. Said questionnaire included questions regarding the internal accounting control of Nay and First Securities. Ernst & Ernst failed to discover that Nay and First Securities lacked proper internal accounting controls, including the controls required by Rule 27 (c) aforesaid or, if they did learn it, failed to disclose such failure in its answers to said questionnaire, thereby permitted Nay and First Securities Company to defraud the plaintiffs as aforesaid.

8. By such failure as aforesaid the defendant, Ernst & Ernst, aided and abetted the aforesaid violations by Nay of Section 10 of the Securities & Exchange Act of 1934 and Rule 10 b-5 of the Securities and Exchange Commission as aforesaid.

9. Plaintiffs have been required to employ attorneys to present this claim and prosecute this action. Plaintiffs are entitled to recover for the reasonable services of such attorneys.

Wherefore, plaintiffs demand judgment against the defendant, Ernst & Ernst, for Nine Hundred Seventy-Two Thousand Five Hundred ($972,500) Dollars; for a reasonable fee for plaintiff's attorneys; for the costs of this action and; for all other relief as may be just and proper in the premises.

/s/ King, Robin, Gale & Pillinger

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IN THE UNITED STATES DISTRICT COURT

• • (Caption — No. 71 C 454) • •

ANSWER OF ERNST & ERNST TO FIRST AMENDED COMPLAINT

(August 24, 1972)

Defendant, Ernst & Ernst, by its attorneys, Michel A. Coccia, Robert L. Berner, Jr., and Michael J. Madda, answers the First Amended Complaint (the allegations of which are quoted below in brackets) as follows:

FIRST COUNT

Ernst & Ernst is not charged as a Defendant in the First Count.

SECOND COUNT

[1. At all times hereinafter mentioned the defendant, Ernst & Ernst was a partnership with an office in Chicago, Illinois, engaged in the profession of Certified Public

Accounting under the Illinois statutes and so held itself out to the public.]

1. Ernst & Ernst admits the allegations of paragraph 1.

[2. Plaintiffs bring this action under §10 of the Securities Exchange Act of 1934, as amended, 15 U.S.C. §78 j. This Court has jurisdiction thereof under §27 of the Securities Exchange Act of 1934, as amended, 15 U.S.C. §78 aa.]

2. Ernst & Ernst admits that plaintiffs purport to bring this action under Sections 10 and 27 of the Securities Exchange Act of 1934, as amended (hereinafter the "Exchange Act"). Ernst & Ernst denies the applicability of Section 10 of the Exchange Act to this action, and denies that this court has jurisdiction of plaintiffs' claims under Section 27 of the Exchange Act.

[3. Plaintiffs prior to June 1, 1968 were securities customers of First Securities Company of Chicago, a securities dealer with offices on LaSalle Street in Chicago, the President of which, and the owner of 92% of the stock of which, was Leston B. Nay, a member of the Midwest Stock Exchange.]

3. Ernst & Ernst admits that, at certain times, First Securities Company of Chicago (hereinafter "First Securities") was a securities dealer with offices on LaSalle Street in Chicago, Illinois, and the President of which, and the owner of 92% of the stock of which, was Leston B. Nay (hereinafter "Nay"). Ernst & Ernst is without knowledge or information sufficient to form a belief as to the truth of the allegation that all plaintiffs at all times prior to June 1, 1968 were securities customers of First Securities and therefore denies said allegation. Ernst & Ernst denies that Nay was a member of the Midwest Stock Exchange (hereinafter the "Exchange").

Ernst & Ernst denies the remaining allegations of paragraph 3.

[4. Nay fraudulently persuaded each of the plaintiffs to sell his securities through First Securities Company of Chicago and fraudulently persuaded each of them to invest the proceeds, aggregating $972,500 as to all plaintiffs, in a fictitious and non-existent escrow and issued to each of them a security for said investment on the letterhead of First Securities Company, Member Midwest Stock Exchange. Nay converted their said money to his own use immediately upon its receipt. In so defrauding each of the plaintiffs, Nay used the mails, the public telephone system and the facilities of National Securities Exchanges. Nay shot and killed himself in June, 1968. His estate has no assets and First Securities Company of Chicago is insolvent.

Nay's said fraud violated Section 10 b of the Securities Exchange Act of 1934 and Rule 10 b-5 of the Securities Exchange Commission promulgated under the authority of said Section 10 of the Securities Exchange Act of 1934, 15 U.S.C. Section 78 j.]

4. Ernst & Ernst admits that Nay shot and killed himself in June, 1968. Ernst & Ernst denies the remaining allegations of paragraph 4.

[5. Rule 10 b-5 aforesaid, 17 Code of Federal Regulations, §240.10 b 5, 1968, promulgated by the Securities Exchange Commission under Section 10 of the Securities Exchange Act of 1934 provides as follows:

"It shall be unlawful for any person directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud.

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security."]

5. Ernst & Ernst admits that paragraph 5 correctly sets forth the provisions of Rule 10b-5 of the Securities and Exchange Commission (the "Commission") promulgated under Section 10 of the Exchange Act, but denies its applicability to this action.

[6. The defendant, Ernst & Ernst, aided and abetted Nay in his violation of the Rule and Act aforesaid, among others, in the following ways:]

6. Ernst & Ernst denies that it aided and abetted any violation by Nay of Section 10 of the Exchange Act or Rule 10b-5 of the Commission.

[6(a). For several years prior to June 1, 1968, Ernst & Ernst, as Certified Public Accountants, were employed by Nay and First Securities Company to furnish to the Midwest Stock Exchange an annual surprise audit of First Securities Company as required by the rules of the Midwest Stock Exchange. Ernst & Ernst, as Certified Public Accountants, knew, or should have known, that the purpose of said audit was to enable the Midwest Stock Exchange to continue to represent to the public that Nay, as a member of the Midwest Stock Exchange, was a person with a high standard of commercial honor and integrity and that the purpose of such audit report

was, therefore, to protect customers of Nay and First Securities Company against loss by fraud.]

6(a). Ernst & Ernst admits that for several years prior to June 1, 1968, it was employed as independent public accountants by First Securties under approval from the Exchange to conduct an annual audit of First Securities, which audit for the years 1963 through 1967 was conducted as a surprise audit pursuant to the Rules of the Exchange. Ernst & Ernst denies the remaining allegations of paragraph 6(a).

[6(b). Ernst & Ernst knew, or should have known, that investors in dealing with Nay and First Securities Company would rely on Nay's membership in the Midwest Stock Exchange, as the plaintiffs did rely, and that the continuance of said membership was dependent on the accuracy and completeness of the surpise audit report by Ernst & Ernst to the Midwest Stock Exchange.]

6(b). Ernst & Ernst denies the allegations of paragraph 6(b).

[6(c). Ernst & Ernst failed to exercise proper or appropriate auditing procedures in making said audit of First Securities Company among others in the following respects:]

6(c). Ernst & Ernst denies that it failed to exercise proper and appropriate auditing procedures in connection with any audit by it of First Securities.

[6(c)(i). Under standard auditing practice it was the duty of Ernst & Ernst as such auditors to make adequate and proper inquiry on whether the officers and employees of First Securities Company took regular vacations, and whether during such vacations their duties were performed by other employees; and Ernst & Ernst failed to make such inquiry and failed to discover that Nay, the president of the company, took no regular vacations;

and that the mail addressed to the Company piled up unopened on his desk when, for a single day or more, he was absent from the office, and thus Ernst & Ernst failed to discover that First Securities had no adequate or proper accounting control.]

6(c)(i). Ernst & Ernst denies the allegations of paragraph 6(c)(i).

[6(c)(ii). Under standard auditing practice it was the duty of Ernst & Ernst as such auditors to make adequate and proper inquiry on the standard rules of First Securities Company regarding the opening of mail, and Ernst & Ernst failed to make such inquiry and failed to discover that Nay as president of the company required that all mail addressed to the Company for his attention be opened only by him and thus failed to discover that the company had no adequate or proper accounting control.]

6(c)(ii). Ernst & Ernst denies the allegations of paragraph 6(c)(ii).

[6(c)(iii). Ernst & Ernst knew, or should have known, that Nay took no regular vacations and forbade the officers and employees of First Securities Company to open any mail addressed to him or to First Securities Company for his attention and that he thus kept secret from the other officers of First Securities Company the considerable correspondence that he had with the plaintiffs in perpetrating said fraud, much of which was on the letterheads of First Securities Company, "member of Midwest Stock Exchange". This procedure violated Rule 27 (c) of the National Association of Securities Dealers, a body organized under statutory authority to perform, under oversight of the Securities and Exchange Commission, regulatory functions, which provided as follows:

"(c) Each member shall be responsible for keeping and preserving appropriate records for carrying out the member's supervisory procedures. Each member shall review and endorse in writing, on an internal record, all transactions and all correspondence of its registered representatives pertaining to the solicitation or execution of any securities transaction."

Despite the fact that Nay and First Securities Company were members of said National Association of Securities Dealers and that the procedure required by the foregoing rule constitutes the standard of the securities industry, no effort whatever was made by Nay or First Securities Company to comply with the foregoing rule and it was the duty of Ernst & Ernst as Certified Public Accountants to report said failure to the Midwest Stock Exchange, and Ernst & Ernst as such auditors failed to report in its said audit reports to the Midwest Stock Exchange such non-compliance with said rule, thus omitting to state a material fact in its said audit reports, and the losses of the plaintiffs as aforesaid resulted from such failure.]

6(c)(iii). Ernst & Ernst admits that paragraph 6(c)(iii) correctly sets forth the provisions of Section 27(c) of the Rules of Fair Practice of the National Association of Securities Dealers, Inc. Ernst & Ernst denies the remaining allegations of paragraph 6(c)(iii).

[7. Under the terms of the employment of Ernst & Ernst as Certified Public Accountants to make such audit, it was the duty of Ernst & Ernst to prepare and file with the Midwest Stock Exchange an answer to the Midwest Stock Exchange's financial questionnaire. Said questionnaire included questions regarding the internal accounting control of Nay and First Securities. Ernst & Ernst failed to discover that Nay and First Securities

lacked proper internal accounting controls, including the controls required by Rule 27(c) aforesaid or, if they did learn it, failed to disclose such failure in its answers to said questionnaire, thereby permitted Nay and First Securities Company to defraud the plaintiffs as aforesaid.]

7. Ernst & Ernst admits that it was employed by First Securities to prepare for filing with the Exchange, in connection with its annual audits of First Securities pursuant to the Rules of the Exchange, the Exchange's financial questionnaire with respect to First Securities, and it admits that this questionnaire included questions regarding the internal accounting control of First Securities. Ernst & Ernst denies the remaining allegations of paragraph 7.

[8. By such failure as aforesaid the defendant, Ernst & Ernst, aided and abetted the aforesaid violations by Nay of Section 10 of the Securities & Exchange Act of 1934 and Rule 10 b-5 of the Securities and Exchange Commission as aforesaid.]

8. Ernst & Ernst denies that it aided and abetted and abetted any violation by Nay of Section 10 of the Exchange Act or Rule 10b-5 of the Commission. Ernst & Ernst denies that any conduct of Nay violated such provisions, and it denies any liability thereunder to plaintiffs, or any of them, by reason of any facts alleged in the Second Count or for any other reason.

[9. Plaintiffs have been required to employ attorneys to present this claim and prosecute this action. Plaintiffs are entiled to recover for the reasonable services of such attorneys.]

9. Ernst & Ernst admits that plaintiffs have employed attorneys, but it denies the remaining allegations of paragraph 9.

FIRST DEFENSE

The Second Count fails to state a claim upon which relief can be granted against Ernst & Ernst.

SECOND DEFENSE

This court lacks jurisdiction over the subject matter of plaintiffs' claims against Ernst & Ernst in the Second Count.

THIRD DEFENSE

Ernst & Ernst had no knowledge of any conduct of Nay alleged to be fraudulent in the Second Count. Without such knowledge, Ernst & Ernst could not aid or abet Nay's alleged fraudulent conduct.

FOURTH DEFENSE

Plaintiffs dealt with Nay as an individual on a personal basis with respect to the allegations of the Second Count, and plaintiffs did not deal with First Securities in connection therewith. No duty was thus owed to plaintiffs by Ernst & Ernst with respect to such allegations.

FIFTH DEFENSE

Ernst & Ernst exercised due diligence and care and took all required and appropriate steps under generally accepted auditing standards, all applicable laws, rules or regulations, or otherwise in connection with all audits by it of First Securities, including, but not limited to, confirmation with all customers of First Securities, including plaintiffs, of their securities accounts and cash positions with First Securities in the normal course of each such audit. The alleged fraudulent conduct of Nay was not, and could not reasonably have been, discovered

or known by Ernst & Ernst in the exercise of such due diligence and care and the taking of such required and appropriate steps.

SIXTH DEFENSE

No damage suffered by plaintiffs as alleged in the Second Count was caused by Ernst & Ernst.

FIRST AFFIRMATIVE DEFENSE

In connection with its annual audits of First Securities, Ernst & Ernst confirmed the securities accounts and cash positions of all customers of First Securities, including certain plaintiffs, directly with them by means of confirmation letters. No plaintiff at any time informed Ernst & Ernst, in connection with the confirmation of their accounts and cash positions or otherwise, of any aspect of the alleged "escrow" transactions or of Nay's alleged conduct, and no plaintiff, at any time, complained to Ernst & Ernst or, to the knowledge of Ernst & Ernst, to First Securities or any other person or entity that printed confirmations of sale were not mailed to them by First Securities in connection with the alleged "escrow" transactions. Plaintiffs' failure to so inform Ernst & Ernst estops them from asserting any liability against Ernst & Ernst in connection with the allegations of the Second Count.

SECOND AFFIRMATIVE DEFENSE

If plaintiffs, or any of them, have stated a cause of action in the Second Count, some or all of the several claims stated therein accrued more than three years prior to February 19, 1971, the date of the commencement of this suit, or plaintiffs, or any of them, should have

discovered the existence of such cause of action in the exercise of ordinary diligence more than three years prior to February 19, 1971, the date of the commencement of this suit. Some or all of the several claims alleged in the Second Count are therefore barred by the applicable statute of limitations.

Wherefore, defendant Ernst & Ernst respectfully prays that the Second Count be dismissed and that costs be assessed against the plaintiffs.

BAKER & McKENZIE

By: .....

Attorneys for Defendant
Ernst & Ernst

700 Prudential Plaza
Chicago, Illinois 60601
312-828-0400

RESPONDENTS' ANSWERS AND SUPPLEMENTAL ANSWERS TO CERTAIN INTERROGATORIES OF PETITIONER

(February 29, 1972; July 13, 1972; October 19, 1972)

13. State (a) the date upon which you first became a securities customer of First Securities (other than by your alleged investment in the "escrow") and/or the dates of the commencement of each brokerage account (other than in connection with the "escrow") ever maintained with First Securities, (b) how you came to be such a customer of First Securities and the circumstances surrounding the opening of each such brokerage account with First Securities, (c) the nature of each such account with First Securities (cash, margin, discretionary, or other), and (d) the date you terminated each such account

with First Securities and/or ceased to be such a customer of First Securities.

JOINT AND SEVERAL ANSWER OF ALL RESPONDENTS TO QUESTION 13:

In response to your formal request for pertinent documents, all of this information was on December 15, 1971 furnished to you by us in great detail in the transcripts of our sworn testimony before Master Charles A. Bane in case 68 C 1053 in this Court and in the many exhibits which we then produced and furnished you. Those transcripts and exhibits are hereby incorporated herein as our several answers to the foregoing Interrogatory.

Those exhibits are our business records of the transactions involved here and we hereby specify them as a sufficient answer to the above Interrogatory under Rule 33, (c) of the Rules of Civil Procedure for the United States District Courts.

ANSWERS TO QUESTION 13.

Leon S. Martin (a) About 1941. (b) Recommended by Dorothy Hess, deceased. (c) Cash (d) Terminated June 6, 1968.

L. Stanbridge Martin (a) About 1960. (b) Leon S Martin, Sr. (c) Cash (d) June 6, 1968.

SUPPLEMENTARY ANSWER TO QUESTION 13 AT THE REQUEST OF ERNST & ERNST:

Leon S. Martin—Dorothy Hess worked with my wife at the University of Chicago as a secretary. She recommended Nay to me as a good, honest, competent stockbroker. On her recommendation I went to his office and had him buy certain stocks which he recommended.

ANSWER OF OLGA HOCHFELDER TO INTERROGATORY 13:

a) 1951.
b) At that time I had some money to invest, $9,000 from the sale of a building, and my boss at the time, Mr. W. H. Rothermel, advised me to go to his friend, Mr. Nay. He advised me to invest in mutual funds, and as a result made three such purchases for me at that time.
c) Cash.
d) June 1968.

ANSWER OF AGNES SMITH TO INTERROGATORY 13:

a) 1951.
b) Nay, who I had met socially, called me from his office and asked me how I was getting along. I told him I was in somewhat financial straits, and he asked if First Securities Company could be of some help. I went to Nay's office and began buying and selling securities on his advice.
c) Cash.
d) 1968.

ANSWER OF EUGENE VOITA TO INTERROGATORY 13:

a) Late 1947.
b) I had been dealing with Mr. Kenneth Clark at Harris Upham & Co. for several years. Mr. Clark was retiring, and at his suggestion I let him turn my account over to Nay at First Securities, whom he had known personally for many years.
c) Cash.
d) 1968.

ANSWER OF ANNA L. JESSE TO INTERROGATORY 13:

a) 1954.
b) I had known Nay on a social basis for about nine years prior to 1954. I inherited, from my mother, a large number of stocks, so I went to Nay at the First Securities Co. for advice on investments. Nay advised me to diversify my holdings, and I took his advice, dealing through First Securities.
c) Cash.
d) 1968.

ANSWER OF WILLIAM P. JESSE TO INTERROGATORY 13:

Same as Anna L. Jesse.

ANSWER OF THERESA W. ROTHERMEL TO INTERROGATORY 13:

a) 1948.
b) I knew Mrs. Nay, and Mr. Nay slightly at that time. My husband and I wanted to invest some money so we checked and found First Securities to be a reputable firm and a member of the Midwest Stock Exchange. Therefore, we felt safe making investments through them. We went to the company and took Nay's advice in investing.
c) Cash.
d) 1968.

ANSWER OF HELEN C. ALLISON TO INTERROGATORY 13:

a) Shortly after September 15, 1965, the date of my husband's death, I had one brokerage account.

b) My husband had been a customer of First Securities. After my husband's death, Leston Nay was considerate, thoughtful, and kind. When I received a $40,000 insurance check, I called Mr. Nay to ask him what to do with it. He gave me his advice and opened my First Securities account.
c) I believe it was an ordinary cash account.
d) I never formally terminated the account. Of course, I ceased to be a customer of First Securities when Leston Nay killed himself. My last transaction with the company was their sale of some stock for me in the latter part of March, 1968, on which I received the sale proceeds in the early part of April, 1968.

ANSWER OF LURENA STUBBS TO INTERROGATORY 13:

a) March 1954.
b) Our stockbroker, Paul H. Davis, combined with Hornblower & Weeks. My husband and I felt we no longer had the same connection with Davis, so we transferred to Nay and the First Securities Co. We knew Nay socially and people had recommended him as an investment counselor.
c) Cash.
d) 1968.

ANSWER OF JOHN M. JACKSON TO INTERROGATORY 13:

To the best of my recollection and so far as my records indicate, my first transaction with First Securities Company was December 15, 1942, although I think First Securities succeeded to the business of Ryan, Nichols & Company, and if First Securities Company com-

menced doing business under that name prior to December 15, 1942, I may have had some prior transactions.

Subsequently, I opened the following accounts with First Securities Company. The dates are those reflected in the earliest records I can find as to each account:

John M. Jackson and Elizabeth B. Jackson—December 24, 1952;

John M. Jackson, Executor U/W William H. Jackson, deceased—March 12, 1958;

John M. Jackson, Trustee U/W William H. Jackson, deceased—October 8, 1958.

I became such a customer because my father was of the opinion that Nay was always associated as an employee or principal with reputable, substantial brokerage firms and considered First Securities to be such a firm. My father introduced me to Nay and took me to First Securities to acquaint me with its offices and facilities. I had no margin or discretionary accounts but maintained a cash account with First Securities. Although I did not give First Securities discretionary authority, I relied on it, acting through Nay in particular transactions and probably gave limited oral discretionary authority as one might do to any responsible brokerage firm. I ceased to be a customer of First Securities and terminated my accounts with it when the firm closed.

ANSWER OF ELIZABETH TO INTERROGATORY #13:

My first dealings with First Securities, so far as I can recall, was when it held a security of mine in safekeeping in 1949. My first substantial dealings were in 1963. The only accounts I had with First Securities were cash accounts. One was a joint account with John M. Jackson (see answer of John M. Jackson) and the other was a

personal account which, according to the records, I can find, was opened on June 9, 1965 and in which I had transactions until December, 1967. I do not know if the account was closed then but I think I had no more transactions in it, so I presume it was. I had only a cash account. I gave First Securities Company no discretion although I relied substantially on its being a large LaSalle Street broker and a member of a Stock Exchange and on Leston B. Nay as its president.

ANSWER OF JOHN M. JACKSON, TRUSTEE, TO INTERROGATORY #13:

The answer of trustee to Interrogatory #13 is necessarily the same as that of John M. Jackson to that interrogatory. The trust had only a cash account. It had no discretionary account, although limited discretion was given First Securities from time to time on an individual transaction basis as one might give it to any reputable brokerage firm. The account was terminated when First Securities closed.

CARNOVSKY—Interrogatory 13(a), (b), (c) and (d): I first became a customer of First Securities, other than by investment in the escrow, on or about June 21, 1966. I became a customer in the following manner: As related more fully in my testimony on November 20 and 21, 1969, before the Master in Securities Exchange Commission v. First Securities Company of Chicago, No. 68 C 1053, I first met Leston B. Nay about the year 1950 in a social group in the Hyde Park area in Chicago. In the course of social meetings of this group, I learned of Nay's connection with First Securities. In June 1965, I owned 1200 shares in Stein Roe Farnum Balanced Fund. As I testified before the Master, page 172, Nay suggested to me that I had better give "us" those Stein

Roe shares, saying that it would give "you and us" a great deal more flexibility. "We will keep those shares in our box at First Securities." I deposited my 1200 shares of Stein Roe Farnum with First Securities on June 21, 1966 and received a receipt introduced as Exhibit 10 before the Master. At that time Nay asked me to sign a Stock Power and I did so. Subsequently, at Nay's suggestion, the 1200 shares of Stein Roe stock were divided up into five certificates of 240 shares each, each in joint tenancy, one of the joint tenants being myself, and the other joint tenant a person whom I designated. See Exhibit 13. In August 1966, as related more fully in my testimony before the Master at page 179 and following, Nay persuaded me to sell my 1200 shares of Stein Roe Farnum on the pretext that he was worried about the stock market and a repetition of 1929. Acting on his advice, I agreed to the sale of my Stein Roe Farnum stock and it was sold through First Securities on August 23, 1966. See Exhibit 14. The proceeds of $23,808 were transmitted by First Securities to my account at University National Bank. See Exhibit 16. A few days later Nay persuaded me to invest the Stein Roe Farnum proceeds in the escrow and I agreed to do so. Actually I invested the proceeds and a small additional sum as shown by my check of August 27, 1966 for $25,000, Exhibit 17. See also my letter of transmittal of August 27, 1966 and Nay's acknowledgment on the bottom of the check, Exhibit 18.

DRAKE—Interrogatory 13(a), (b), (c), and (d): I was a securities customer of First Securities through my investment in the escrow account. Further, I am the widow of Joseph A. Drake who died in December 1953. I married Joe on August 8, 1943.

First Securities was originally incorporated on March 25, 1939 as George F. Ryan & Co. It changed its name to Ryan-Nichols & Co. on March 24, 1941 and to First Securities on June 24, 1944. (In these answers First Securities is referred to as such even for periods prior to adoption of this name.)

According to papers in my possession, it appears that my husband bought and sold securities in substantial volume through First Securities from 1939 to 1945, about $6,000 in 1939, gradually increasing to about $78,000 in 1945. In 1945 Joe had about $30,000 invested through First Securities. Beginning about 1942, Joe made his first investment in the escrow account. Later I invested money too. We gradually increased our investments so that at the time of Joe's death in 1953 we had invested $40,000. In 1954 Nay repaid $30,000, leaving $10,000 due. So far as I can determine from documents in my possession, it appears that Joe sold the securities which he had purchased through First Securities and over a period of years invested them in the escrow.

For more complete details of the escrow swindle, see the Stipulation Regarding Testimony of Zerah A. Drake in Case No. 68 C 1053 in this court. A copy (without exhibits) is attached hereto.

ANSWER OF HELEN FELDKAMP TO QUESTION 13:

a)b) My husband, who died in 1947, left me with a few stocks and many government bonds, which I wanted to convert to income producing investments. At my request, the Federal Reserve Bank of Chicago gave me the names of three brokerage firms, none of which I knew. Quite at random, I chose the First Securities Co., and went to their offices. There, in 1948, I met with Nay, who advised me on my investments.

c) Cash.
d) 1968.

15. List in chronological order all purchases and sales of securities (other than securities evidencing your alleged investment in the "escrow") made for your account through First Securities, and, with respect to each purchase or sale, state (a) the date, (b) the total dollar amount (c) the individual or individuals connected with First Securities with whom you dealt, and (d) whether each was initiated by yourself or was made on the recommendation of the individual connected with First Securities.

JOINT AND SEVERAL ANSWER OF ALL RESPONDENTS TO QUESTION 15.

In response to your formal request for pertinent documents, all of this information was on December 15, 1971 furnished to you by us in great detail in the transcripts of our sworn testimony before Master Charles A. Bane in Case 68 C 1053 in this Court and in the many exhibits which we then produced and furnished you. Those transcripts and exhibits are hereby incorporated herein as our several answers to the foregoing Interrogatory.

Those exhibits are our business records of the transactions involved here and we hereby specify them as a sufficient answer to the above Interrogatory under Rule 33. (c) of the Rules of Civil Procedure for the United States District Courts.

JOINT ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 15

In response to your formal request for pertinent documents, all of this information was on December 15, 1971 furnished to you by us in great detail in the many

exhibits which we then produced and furnished you. These exhibits are hereby incorporated herein as our answers to the foregoing Interrogatories. These exhibits are our business records of the transactions involved here and we hereby specify them as sufficient answer to the above Interrogatory under Rule 33 (c) of the Rules of Civil Procedure for the United States District Courts.

ANSWER OF OLGA HOCHFELDER TO INTERROGATORY 15:

a) 8/21/51.
b) Purchase 1) 40 shrs Massachusetts Investors Trust $1634.00
2) 100 shrs Fidelity Fund 1888.00
3) 125 shrs Diversified Investment Fund 1831.25
c) and d) Made on recommendation of Nay.
a) 11/5/52.
b) Purchase 30 shrs. Fundamental Investors com. $ 645.90
c) and d) Made on recommendation of Nay.
a) 3/12/53.
b) Purchase 25 shrs. Wisconsin Public Service $ 512.50
c) and d) Made on recommendation of Nay.
a) 10/4/56.
b) Purchase 50 shrs. Columbia Gas System, Inc. $ 876.63
c) and d) Made on recommendation of Nay.
a) 5/9/56.
b) Sale 100 shrs. Burry Biscuit $ 610.08
c) and d) Made on recommendation of Nay.
a) 10/25/60.
b) Sale 100 shrs. C., M. SP. & P. RR. $1399.86
c) and d) Made on recommendation of Nay.

a) 10/2/62.
b) Sale 100 shrs. C., M. SP. & P. RR $ 784.66
c) and d) Made on recommendation of Nay.
a) 12/8/64.
b) Sale 1) 50 shrs. Kratler Corp. $ 408.09
2) 20 shrs. Brunswick Corp. 153.91
3) 12 shrs. Phoenix Steel Corp. 174.75
c) and d) Made on recommendation of Nay.
a) 2/12/65.
b) Purchase 75 shrs. Vapor Corp. $2615.63
c) and d) Made on recommendation of Nay.
a) 3/8/65.
b) Purchase 50 shrs. Kratler Corp. $ 535.55
c) and d) Made on recommendation of Nay.
a) 6/4/65.
b) Purchase 25 shrs. Vapor Corp. $ 939.55
c) and d) Made on recommendation of Nay.
a) 8/16/67.
b) Sale 50 shrs. Eastern Massachusetts St. Railway Adjustment stock $ 977.18
c) and d) Made on recommendation of Nay.
a) 9/5/67.
b) Sale 96 shrs. Countrywide Realty, Inc. $ 160.49
c) and d) Made on recommendation of Nay.
Other stock sold upon Nay's suggestion; no records of these transactions.

ANSWER OF AGNES SMITH TO INTERROGATORY 15:

a) August 5, 1948.
b) Purchase 100 shrs. Industrial Brownhoist com. $1075.00
Purchase 75 shrs. Serrick Corp. 950.44
Purchase 75 shrs. Std. Rwy. Equip. Mfg. com. 1303.13

c) and d) Made on recommendation of Nay.
a) July 17, 1951.
b) Purchase 150 shrs. North Western Pub. Service 1687.50
Purchase 50 shrs. Minnesota & Ontario Paper 1400.25
Purchase 100 shrs. Nash Kelvinator 1831.56
Purchase 150 shrs. Central Gas & Electric 1650.00
Purchase 150 shrs. Mickelberrys Food Products 1373.50
Purchase 100 shrs. Toledo Edison 1063.09
Purchase 10 shrs. AT&T 1556.60
Purchase 50 shrs. Rockwell Mfg. Co. 1375.00
Purchase 150 shrs. Interstate Motor Freight 1631.25
Purchase 50 shrs. Toledo Edison 539.37
c) and d) Made on recommendation of Nay.
a) July 18, 1951.
b) Purchase 70 shrs. E. L. Bruce & Co. com $1584.08
c) and d) Made on recommendation of Nay.
a) July 23, 1951.
b) Purchase 50 shrs. Serrick Corp. $ 737.25
c) and d) Made on recommendation of Nay.
a) July 24, 1951.
b) Purchase 2 shrs. AT&T $ 319.37
c) and d) Made on recommendation of Nay.
a) August 24, 1951.
b) Purchase 75 shrs. Petroleum Heat & Power $1415.63
Purchase 75 shrs. Blacksivalls & Bryson 1387.50
c) and d) Made on recommendation of Nay.
a) May 13, 1952.

b) Sale 150 shrs. Interstate Motor Freight $1679.90
Sale 100 shrs. Industrial Brownhoist 969.95
Sale 150 shrs. Central Electric & Gas 1679.70
Sale 150 shrs. Northwestern Pub. Service 1650.00
Sale 50 shrs. Minnesota & Ontario Paper 1188.57
Sale 50 shrs. Toledo Edison 534.18
Sale 75 shrs. Standard Ry. Equipment 1008.20
Sale 75 shrs. Petroleum Heat & Power 1288.65
Sale 100 shrs. Toledo Edison 1084.22
c) and d) Made on recommendation of Nay.
a) May 27, 1952.
b) Sale 25 shrs. Serrick Corp. $ 344.69
Sale 100 shrs. Serrick Corp. com. 1390.74
Sale 75 shrs. Black Sivalls & Bryson com. 1307.45
c) and d) Made on recommendation of Nay.
a) July 15, 1952.
b) Sale 12 Rts. AT&T $ 23.96
c) and d) Made on recommendation of Nay.
a) September 23, 1952.
b) Sale 100 shrs. Nash Kelvinator com. $2016.96
Sale 50 shrs. Rockwell Mfg. Co. com 1339.35
Sale 70 shrs. E. L. Bruce & Co. com. 1235.09
Sale 12 shrs. AT&T 1829.24
Sale 150 shrs. Mickelberrys Food Products 1177.87
c) and d) Made on recommendation of Nay.
a) September 22, 1953.
b) Sale 11 shrs. C. A. Durham Co. Ltd. com. $ 109.40
Sale 1 shr. American Funding Corp. com. 1.95
c) and d) Made on recommendation of Nay.
a) September 23, 1953.
b) Sale 231 shrs. C. A. Durham & Co. com. $ 956.36
Sale 10 shrs. C. A. Durham & Co. com. 40.45
c)and d) Made on recommendation of Nay.

ANSWER OF EUGENE VOITA TO INTERROGATORY 15:

a) September, 1947.
b. Purchase 100 shrs. Tucker Corp.
c) and d) Made on recommendation of Nay.
a) May, 1948.
b) Purchase 230 shrs. Group Aviation Corp.
c) and d) Made on recommendation of Nay.
a) May, 1948.
b) Sale 25 shrs. Am. Airlines
c) and d) Made on recommendation of Nay.
a) May, 1948.
b) 220 shrs. Cincinnati Gas & Electric Co.
c) and d) Made on recommendation of Nay.
a) June, 1948.
b) Sale 100 shrs. Erie Ry. Co.
c) and d) Made on recommendation of Nay.
a) July, 1948.
b) Sale 100 shrs. Cincinnati Milling Machine Co.
c) and d) Made on recommendation of Nay.
a) June, 1948.
b) Purchase 100 shrs. B & O Ry.
c) and d) Made on recommendation of Nay.
a) January, 1949.
b) Purchase 100 shrs. Minnesota Ontario Paper Co.
c) and d) Made on recommendation of Nay.
a) January, 1949.
b) Purchase 150 shrs. Berkshire Finishing Co.
c) and d) Made on recommendation of Nay.
a) January, 1949.
b) Purchase 170 shrs. Dayton Malleble Iron Co.
c) and d) Made on recommendation of Nay.
a) February, 1949.

b) Purchase 150 shrs. Texas Eastern Transmission Gas Pipe Line
c) and d) Made on recommendation of Nay.
a) March, 1949.
b) Purchase 125 shrs. Maryland Casualty Co.
c) and d) Made on recommendation of Nay.
a) May, 1949.
b) Purchase 200 shrs. Cleveland Cliffs Iron Co.
c) and d) Made on recommendation of Nay.
a) June 9, 1959.
b) Purchase 40 shrs. Livingston Oil Co.
c) and d) Made on recommendation of Nay.
a) January, 1949.
b) Sale 100 shrs. Cities Service Co. and 100 shrs. Marathon Co.
c) and d) Made on recommendation of Nay.

ANSWER OF ANNA L. JESSE TO INTERROGATORY 15:

a) 1955.
b) Sale Commonwealth Edison, Duquesne Power & Light, Fdelity Company, Fundamental Investors, Massachusetts Investors.
c) and d) Made on recommendation of Nay.
a) February 17, 1955.
b) Purchase 94 shrs. Quaker Oats com $3083.58
c) and d) Made on recommendation of Nay.
a) June 8, 1959.
b) Sale 1040 shrs. Livingston Oil Co. 2041.76
c) and d) Made on recommendation of Nay.
a) July 2, 1959.
b) Sale $18,000 U. S. Treasury 2-½% $14,967.07
c) and d) Made on recommendation of Nay.

a) April 30, 1965.
b) Sale 88 shrs. Chemical Paper Mfg. Corp. com. $3155.40
c) and d) Made on recommendation of Nay.
a) November 18, 1965.
b) Sale 100 shrs. Quaker Oats Co. $7749.92
c) and d) Made on recommendation of Nay.
a) November 18, 1965.
b) Sale 10 shrs. Quaker Oats Co. $764.38
c) and d) Made on recommendation of Nay.
a) November 23, 1965.
b) Sale 414 shrs. AT&T $25,772.67
c) and d) Made on recommendation of Nay.

ANSWER OF WILLIAM P. JESSE TO INTERROGATORY 15:

Same as Anna L. Jesse.

ANSWER OF THERESA W. ROTHERMEL TO INTERROGATORY 15:

a) March 31, 1948.
b) Purchase
50 shrs. Internat. Minerals & Chemical $1497.13
10 shrs. Commonwealth Edison com. 286.18
c) d) Nay.
a) November 18, 1949.
b) Purchase 25 shrs. M.I.T. 718.50
c) d) Nay.
a) August 20, 1958.
b) Purchase
90 shrs. M.I.T. 1126.80
$1000 U. S. Treasury 3-¼% 946.41
$1000 Sheraton Corp. Deb. 5% 1006.81
$1000 Fairbanks Morse 5-¾% 946.08

c) d) Nay.
a) June 10, 1959.
b) Sale $10,000 U. S. Treasury 2-½%
c) d) Nay.
a) April 19, 1962.
b) Purchase
9 shrs. Commonwealth Edison 409.81
36 shrs. M.I.T. 586.08
2 shrs. AT&T 263.05
c) d) Nay.
a) September 13, 1965.
b) Purchase
188 shrs. M.I.T. $3664.12
44 shrs. AT&T 3076.53
44 shrs. Commonwealth Edison 2434.53
c) and d) Nay.
a) October 12, 1966.
b) Sale
100 shrs. AT&T $5218.13
50 shrs. AT&T 2594.81
1 shr. Commonwealth Edison 43.12
Purchase
700 shrs. Selected American Shrs. Inc. com. 7637.00
75 shrs. Consolidated Edison Co. N.Y. 2504.68
200 shrs. Consolidated Edison Co. N.Y. 6646.18
150 shrs. Ill. Bell Telephone Co. com. 7573.80
Sale
200 shrs. Commonwealth Edison Co. com. 9115.81
c) d) Nay.
a) October 13, 1966.
b) Sale 503 shrs. M.I.T. $7539.97
c) d) Nay.
a) August 24, 1967.

b) Purchase

$5000 Ill. Toll Highway 3-¾%	$4730.73
$5000 Pacific Power & Light 4-¾%	4223.30

c) d) Nay.

a) September 22, 1967

b) Purchase

1430 shrs. Mass. Ins. Growth Stock Fd.	$20,062.90
770 shrs. Selected Am. Shrs. com.	11,003.30

c) d) Nay.

a) October 16, 1967.

b) Purchase $10,000 U. S. Treasury Bills $9898.09

c) d) Nay.

a) January 23, 1968.

b) Purchase $10,000 U. S. Treasury Bills $9957.25

c) d) Nay.

a) January 25, 1968.

b) Purchase 823 shrs. Selected American Shares $10,007.68

c) d) Nay.

a) February 20, 1968.

b) Purchase 800 shrs. Selected Special Shares $10,056.00

c) d) Nay.

a) May 21, 1968.

b) Sale

100 shrs. Plough Inc.	$7185.81
100 shrs. Plough Inc.	7148.65
40 shrs. Plough Inc.	2851.51

c) d) Nay.

a) June 3, 1968.

b) Purchase $10,000 U. S. Treasury Bills $9954.79

c) d) Nay.

ANSWER OF HELEN C. ALLISON TO INTERROGATORY 15:

a) b):

Date	Shares	Investments	Purchases	Sales
1965:				
October		U. S. Treasury Bills	$40,000.00	
December 20	100	Keystone Custodian Funds (S-3) (as principal)	2,361.00	
December 21	20	Atchison, Topeka & Santa Fe	694.63	
December 21	60	Southern Cal. Ed. Co.	2,444.38	
December 21	23	General Motors	2,377.67	
December 21	80	Southern Pacific Co.	3,735.80	
December 21	36	Union Oil of Calif.	1,923.29	
December 21	400	Futterman Corp. Class A Common	2,452.00	
December 21	200	Do.	1,200.76	
December 21	100	Do.	600.38	
December 21	100	Do.	600.68	
1966:				
January 25	100	Murphy Pacific Marine Salvage Co. (as principal)	1,000.00	
February 25	20	Union Pacific RR Co.		$ 866.18
February 25	100	Atchison, Topeka and Santa Fe R.R.		3,985.78
February 25	80	Southern Pacific Co.		3,505.22
April 19	74	AT&T		4,170.62
April 19	300	AT&T		17,003.02
1967:				
June 5	50	Murphy Pacific Marine Salvage Co.		836.50
August 22	50	Do.		898.37

1968:				
January 15	1222	Mass. Investors Trust		19,979.70
January 17	842	Value Line Special Situations Fund Inc.	$ 8,495.78	
January 17	496	Do.	5,004.64	
January 18	1076	Selected American Shares	13,503.80	
January 17	948	Keystone S3		9,477.85
January 29	2	Charles Pfizer & Co.		126.99
January 29	4	E. I. duPont deNemours	633.30	
January 29	8	Swift & Co.	239.30	
February 21	80	Mass. Investors Trust		1,207.20
March 22	400	Titan Group		2,793.48
March 22	140	Value Line Special Situation Fund	1,192.80	
March 27	400	Titan Group		3,338.00

c) d) Made on recommendation of Leston B. Nay.

ANSWER OF LURENA STUBBS
TO INTERROGATORY 15:

a) April 30, 1954.
b) Sale

300 shrs. G.W. Helms & Co.	$4,238.56
100 shrs. Snap-On-Tools Corp.	1,950.25
100 shrs. Snap-On-Tools Corp.	1,950.20
200 shrs. Sangamo Electric	5,018.31
180 shrs. Skil Corp.	3,487.97
100 shrs. Bliss & Laughlin	2,243.74
50 shrs. Bliss & Laughlin	1,114.79

a) May 3, 1954.
b) Sale 100 shrs. Bliss & Laughlin $2,268.62
c) d) Made on recommendation of Nay.
a) May 4, 1954.
b) Sale 100 shrs. Mickelberry Foods.
c) d) Made on recommendation of Nay.
a) September 20, 1954.
b) Sale 100 shrs. U. S. Playing Card com. $6,540.52
c) d) Made on recommendation of Nay.
a) March 8, 1955.
b) Sale 100 shrs. International Packers com. $1,451.12
c) d) Made on recommendation of Nay.
a) March 17, 1955.
b) Sale

100 shrs. Harvey Hubbel com.	$3,621.64
200 shrs. Harvey Hubbel com.	7,193.99

c) d) Made on recommendation of Nay.
a) March 18, 1955.
b) Sale

100 shrs. Bendix Corp.	$11,103.32
7 shrs. Bendix Corp.	771.67

c) d) Made on recommendation of Nay.
a) March 25, 1955.
b) Sale 100 shrs. Oak Mfg. Co. com $2,372.89
c) d) Made on recommendation of Nay.
a) March 26, 1955.
b) Sale

2 shrs. Socony Vacuum Oil	$ 107.43
50 shrs. Pullman Co.	3,130.62
100 shrs. Bastian Blessing Co.	6,152.67
100 shrs. Socony Vacuum Oil	5,653.93
2 shrs. Socony Vacuum Oil	97.43

c) d) Made on recommendation of Nay.
a) October 2, 1956.

b) Sale

100 shrs. Los Angeles Transit	$1,516.62
21 Rts. AT&T	135.64
21 shrs. AT&T	3,508.29

c) d) Made on recommendation of Nay.

a) June 8, 1959.

b) Sale 1040 shrs. Livingston Oil	$2,004.36

c) d) Made on recommendation of Nay.

a) October 22, 1954.

b) Purchase 100 shrs. Los Angeles Transit com.	$1,387.50

c) d) Made on recommendation of Nay.

Answer of John M. Jackson individually and as trustee, and of Elizabeth B. Jackson, to INTERROGATORY #15:

Our transactions were too numerous to permit us to recall the data requested, but from the records we have, the following is as complete an answer as we can now give:

(Note — Some of these items were confirmed on acknowledgments of Ryan, Nichols & Co., but since First Securities & Company used the confirmation forms of Ryan, Nichols & Company with a rubber stamp overprint, we assume someone simply neglected to stamp First Securities & Company's name over that of Ryan, Nichols & Company)

John M. Jackson

1942	Purchases	Sales
12-15	$ 1,224.30	$
12-18	9,559.35	
12-29	821.70	
12-31		825.00
1943		
4-24	3,001.05	
	2,997.54	
9-30	2,006.25	
10-7		2,006.25
10-8	2,006.25	
12-1	7,276.00	
1944		
2-29	1,125.00	
6-6	11,304.40	
		12,539.78
6-8		6,673.80
6-10	6,366.10	
8-4		603.60
8-28	1,200.00	
9-5		1,214.90
9-28	2,575.00	
	973.53	
		3,462.50
	1,959.62	
	3,300.00	
	3,018.75	
	2,043.75	
		21,210.75
11-29	1,987.50	
12-5		1,228.08
12-7	2,400.00	
12-13	2,100.00	
12-14		2,400.00
12-16		5,379.51
	2,400.00	
12-18	3,624.00	
		3,787.02

1944	Purchases	Sales
12-19		1,176.59
12-28	2,775.00	
		2,942.60
1945		
2-5		1,424.90
2-20	2,675.00	
	1,200.00	
2-21		1,068.43
		1,442.51
2-23		1,430.03
2-24		2,049.82
3-16	1,900.00	
3-21		1,065.43
		2,105.94
		1,065.43
4-25	1,162.50	
4-30		2,062.26
		1,837.95
5-17	400.00	
6-4		824.85
6-27	2,040.00	
7-5		3,774.70
7-23	2,500.00	
7-27		1,399.50
7-30		1,399.50
9-11		10,958.65
		11,876.34
	4,162.50	
10-17		1,630.28
		1,617.82
		1,642.45
10-30		2,324.90
10-31		1,224.95
11-1		1,237.45
12-5		3,674.50
		2,325.83
		5,693.00
		1,745.50

1946	Purchases	Sales
3-12	1,425.00	
3-18		2,124.90
4-20		1,194.95
4-30		1,530.23
	1,887.50	
	2,511.11	
4-30	2,075.00	
		2,780.54
		2,406.38
		2,979.94
7-1	2,800.00	
7-8	2,437.50	
7-29	3,112.50	
8-6	3,525.00	
9-5	1,162.50	
9-12	3,400.00	
	3,325.00	
		1,694.85
		1,327.20
		789.25
		1,628.37
		1,719.61
9-13	3,200.00	
	4,087.50	
9-16	2,859.38	
		1,881.50
9-17	1,750.00	
9-19	865.50	
		1,657.31
9-20	3,871.11	
9-25		881.90
9-26		3,290.00
9-27	1,737.50	
9-30		792.88
10-1		1,129.50
10-30		575.13
		844.38
		2,471.65
		1,229.72

1946	Purchases	Sales
10-31		1,483.70
	937.50	
		1,383.65
		1,408.59
	2,287.50	
	2,512.50	
	962.50	
	2,575.00	
11-21	2,450.00	
12-4		3.87
		2,292.93
1947		
2-27	2,400.00	
2-28	3,075.00	
	2,325.00	
3-4		3,896.00
3-20		775.00
		3,075.00
9-5		1,477.40
10-22	1,575.00	
	1,500.00	
1947		
10-22	3,100.00	
	787.50	
10-23	1,125.00	
	2,925.00	
		1,239.50
10-27		707.45
		353.70
		1,369.95
		1,369.95
		1,369.95
10-29		207.45
		144.95
11-3		2,759.73
12-20		793.09
1948		
2-17	1,400.00	
		1,382.80

1948	Purchases	Sales
2-27	2,137.50	
	2,850.00	
2-28	1,325.00	
	387.50	
3-8		2,989.68
3-9		1,031.33
		1,031.33
		1,031.33
		149.57
3-12		1,324.50
3-30	840.54	
6-9		2,402.57
		890.45
		2,671.40
6-10		1,942.64
		574.10
6-17	2,325.00	
7-8	1,500.00	
7-26	1,137.50	
10-5	1,400.00	
1949		
1-6		2,331.64
1-8	1,500.00	
1-10	2,325.00	
1-17		744.95
		378.90
1-18		372.45
2-10		1,340.00
	1,350.00	
3-21	1,300.00	
4-7		1,494.80
6-18		1,519.66
	1,509.38	
1950		
3-15	1,620.00	
3-17		1,566.34

1951	Purchases	Sales
1-31		1,801.50
		900.95
	2,653.75	
4-23	2,850.00	
4-24		2,900.28
8-28	2,778.75	
8-29		1,740.00
		1,390.89
12-10		99.90
1953		
1-18		45.49
4-16		827.23
		206.94
1954		
6-28		3,306.40
		1,653.20
		1,640.82
1955		
2-17		89.90
2-23		21.45
1958		
12-2	8,940.30	
1961		
10-23		4,457.01
12-12	4,350.00	
12-18		4,482.81
1963		
1-7		4,457.01
6-5		51.68
1964		
5-27		920.46
		4,479.71
12-8		1,074.00
		207.98

John M. Jackson, Trustee		
1958		
9-16	2,840.75	
	3,479.25	
	2,777.06	
	2,073.75	
	1,073.15	
	2,146.31	
9-17	5,272.98	
	3,806.56	
	1,835.50	
	917.75	
	1,582.50	
	791.25	
	791.25	
	2,531.08	
	2,775.75	
9-18	3,246.50	
1958		
9-19	28,603.02	
	48,162.17	
9-22		1,835.50
		917.75
	914.00	
	1,828.00	
10-8	2,317.17	
1959		
2-13		38,000.00
1960		
2-15		10,000.00
4-25	11,343.75	341.87
		698.07
		19,945.11
9-22	5,650.00	
9-26	2,800.00	
	8.75	
	4,332.06	
9-27	20.28	
	2,166.18	

1959	Purchases	Sales
9-28	4,100.000	
9-29	802.50	
	2,128.30	
		289.93
		287.03
1961		
2-1	8,381.25	
		3,149.25
2-9	6,612.81	
2-10		2,887.44
		2,624.94
2-14		7,366.08
2-15		5,000.00
	2,005.92	
2-21	2,184.75	
2-24		2,240.53
4-28		1,489.22
5-25		1,511.22
		1,272.91
		635.20
6-7		5,747.72
6-9	22,312.50	
6-12		14,088.11
8-2	931.35	
		931.35
8-15		2,571.86
10-25	3,237.50	
		3,131.00
10-30		6,345.21
11-1	2,957.30	
12-4		3,534.56
12-18	14,625.00	
		18,827.81
1962		
8-27		1,050.78
9-20		2,145.62
10-16		7,433.46
		4,361.65
		1,783.93

1962	Purchases	Sales
11-23	15,803.25	
1963		
2-28		2,811.27
6-4		201.29
1964		
1-30		3,568.94
1-31		1,956.48
		873.13
5-22		2,532.53
5-27		3,583.74
6-4		201.29
1965		
6-18		4,652.40
		3,819.69
		2,960.74
		2,948.30
		36.96
		2,948.30
		290.02
		9,125.61
		89.95
		91.95
7-15		
1967		
12-21		6,147.94

1961	Purchases	Sales
6-1	4,331.25	
9-20		8.77
		160.61
10-23	1,428.30	
1962		
10-18		3,922.36
11-21	3,918.75	
1963		
6-26		2,790.75
1964		
5-27		1,816.48
1965		
1-18		3.66
6-18		1,336.88
		776.42
		1,249.30

John M. Jackson and Elizabeth B. Jackson

1960		
10-11	4,050.00	
10-12	3,746.87	

Elizabeth B. Jackson

1965		
6-9		2,515.96
		189.41
		9,747.08
		7,204.68
1967		
12-21		2,330.52
		2,339.27

All dealings (with a couple of exceptions on the part of Elizabeth B. Jackson) with First Securities Company were conducted by John M. Jackson. Most of his dealings in connection with the foregoing transactions were with Leston B. Nay, although there were occasional contacts with Mr. Roy Campbell and Miss Walker. Some of the transactions were initiated by John M. Jackson but he considered Leston B. Nay, as president of First Securities Company, to be his investment advisor and in almost every case the purchases or sales were made on the recommendation of Leston B. Nay. The couple of contacts that Elizabeth B. Jackson had resulted from telephone calls from Leston B. Nay when John M. Jackson was absent from the country. She did precisely what Nay advised her to do.

CARNOVSKY

Interrogatory 15(a), (b), (c), and (d): See my answer to Interrogatory 13. All transactions were initiated on the recommendation of Nay, President of First Securities.

DRAKE

Interrogatory 15(a), (b), (c) and (d): See answer to Interrogatory 13. All my dealings at First Securities were with Leston B. Nay.

ANSWER OF HELEN FELDKAMP TO QUESTION 15:

a) September 30, 1949.
b) Purchase 300 shrs Henry C. Lytton & Co. $2925.00
c) d) Nay.
a) March 16, 1959
b) Sale 100 shrs Henry C. Lytton & Co. $ 956.83
c) d) Nay.
a) April 2, 1959.
b) Purchase $1000 Ill. Toll Highway Commission 4¾% $ 942.80
c) d) Nay.
a) April 16, 1959.
b) Sale 100 shrs. Henry C. Lytton & Co. $1007.33
c) d) Nay.
a) April 17, 1959.
b) Purchase $1000 Ill. Toll Highway Commission 4¾% $ 944.65
c) d) Nay.
a) April 28, 1959.
b) Sale 100 shrs. Henry C. Lytton & Co. $1032.07
c) d) Nay.
a) October 12, 1959.
b) Purchase $1000 Ill. Toll Highway Res. Bnds 4¾% $ 913.85
c) d) Nay.

a) November 9, 1959.
b) Sale 25 shrs. Swift & Co. $1061.88
c) d) Nay.
a) November 16, 1959.
b) Sale $3000 Ill. Toll Highway Commission 4¾% $2710.02
c) d) Nay.

ANSWERS OF LEON S. MARTIN TO INTERROGATORY 15

Purchases

a) 8-8-46
b) 200 shrs. Industrial Brownhoist $2,350.00
a) 9-13-48
b) 13 shrs. Standard Oil of Ind. 570.62
a) 11-30-48
b) 25 shrs. Standard Oil of Ind. 979.55
a) 1-26-51
b) 200 shrs. Pickering Lumber 4,550.00
a) 1-31-51
b) 100 shrs. Pickering Lumber 2,412.50
a) 4-9-51
b) 200 shrs. Lone Star Steel 1,900.00
a) 8-27-51
b) 200 shrs. Pickering Lumber 6,275.00
a) 6-13-52
b) 10 shrs. AT&T 1,526.60
a) 1-26-53
b) 200 shrs. Pickering Lumber 4,550.00
a) 1-29-53
b) 50 shrs. Standard Oil 3,875.78
a) 2-9-53
b) 65 shrs. Commonwealth Ed. 2,344.23

a) 2-19-53	
b) 100 shrs. North Am. Car	$2,195.88
a) 2-9-53	
b) 3 shrs. AT&T	485.81
a) 8-8-55	
b) 550 shrs. Livingston Oil	1,512.50
a) 9-16-57	
b) 200 shrs. Hartford Stores	1,679.00
a) 10-15-57	
b) 30 shrs. Chrysler Corp.	2,214.43
a) 12-3-57	
b) 570 shrs. Livingston Oil	587.10
a) 4-8-59	
b) $10,000.00 Ill. Toll Hwy. Com.	8,057.29
a) 5-24-60	
b) 300 shrs. Kratter Corp.	6,150.00
a) 1-13-61	
b) $7,000.00 U. S. Treas.	6,444.09
a) 1-13-61	
b) $7,000.00 U. S. Treas.	6,375.76
a) 6-2-61	
b) 300 shrs. Kratter Corp.	8,062.50
a) 6-9-61	
b) 600 shrs. Futterman Corp.	7,875.00
a) 6-27-61	
b) 14 shrs. Commonwealth Ed.	1,118.83
c) 7 shrs. AT&T	830.68
a) 5-24-62	
b) 16 shrs. AT&T	1,885.92
a) 9-24-62	
b) $5,000.00 Ill. Tollway Bonds	4,889.06
a) 9-24-62	
b) $25,000.00 Ill. Tollway Bonds	24,445.31
a) 10-16-62	

b) 660 shrs. Futterman Corp.	4,560.05
a) 5-24-62	
b) 16 shrs. AT&T	1,885.92
a) 1-13-61	
b) $7,000.00 U.S. Treasury	6,444.09
7,000.00 U.S. Treasury	6,375.76
a) 7-26-50	
b) 50 shares Group Sec. Aviation	436.70
a) 10-16-57	
b) 50 shrs. Ford Motor	$2,312.58
a) 10-15-57	
b) 572 shrs. Livingston Oil	625.69
a) 3-31-59	
b) 100 shrs. North Amer. Car	6,701.43
c) 20 shrs. North Amer. Car	1,326.00
a) 6-8-60	
b) $7,000.00 Ill. Tollway	6,128.35
a) 9-21-60	
b) 200 shrs. Pickering Lumber	1,544.60
c) 400 shrs. Pickering Lumber	3,089.24
a) 9-21-60	
b) 200 shrs. N. Amer. Car	7,620.26
a) 9-21-60	
b) 570 shrs. Livingston Oil	888.64
a) 9-21-60	
b) 30 shrs. Chrysler Corp.	1,260.41
a) 9-26-60	
b) 200 shrs. Hartfield Stores	1,218.69
c) 6 shrs. Hartfield Stores	34.37
a) 1-13-61	
b) $2,000 U.S. Treasury	2,087.34
c) $5,000 U.S. Treasury	5,239.25
d) $6,000 U.S. Treasury	5,406.64
a) 6-2-21	

b) 300 shrs. Kratter Corp.	7,912.19
a) 9-24-62	
b) 100 shrs. Commonwealth Ed.	4,129.05
c) 100 shrs. Commonwealth Ed.	4,133.35
d) 4 shrs. Commonwealth Ed.	159.91
a) 9-24-62	
b) 100 shrs. Standard Oil of Ind.	4,377.72
c) 100 shrs. Standard Oil of Ind.	4,357.15
a) 9-24-62	
b) 15 shrs. Stand. Oil of N.J.	774.28
c) 9 shrs. Stand. Oil of N.J.	462.56
c) 9-24-62	
b) 100 shrs. AT&T	10,845.52
a) 9-13-62	
b) 600 shrs. Futterman Corp.	4,559.66
a) 3-22-68	
b) 600 shrs. Titan Group	4,690.15
a) 10-16-57	
b) 50 shrs. Ford Motor	2,312.58
a) 3-31-59	
b) 100 shrs. North Am. Car.	6,701.43
c) 20 shrs. North Am. Car.	1,326.00
a) 6-16-54	
b) 100 shrs. Industrial Brownhoist	1,603.70
c) 200 shrs. Industrial Brownhoist	3,256.90
a) 6/2/61	
b) 300 shares Kratter Corp.	7,912.19
a) 6-8-60	
b) $7,000 Ill. State Toll Hwy.	6,128.35
a) 9-21-60	
b) 200 shares Pickering Lumber	1,544.60
c) 400 shares Pickering Lumber	3,089.24
d) 200 shares North Am. Car	7,620.26
e) 570 shares Livingston Oil	888.64
f) 30 shares Chrysler Corp.	1,260.41

SALES

a) 7-26-50	
b) 250 shares Group Sec. Aviation	$1,820.00
a) 7-27-50	
b) 100 shrs Berkshire Fine Spin	1,676.50
a) 8-30-51	
b) 160 shrs. Black, Sivalls & Bryson	2,939.90
a) 10-23-52	
b) 50 shrs. Gerity Mich. Corp.	157.44
a) 10-23-52	
b) 100 shrs. Gerity Mich. Corp.	326.79
a) 12-22-52	
b) 200 shrs. Pickering Lumber	4,133.22
a) 2-9-53	
b) 175 shrs. Rothmoor Corp.	684.20
a) 2-9-53	
b) 100 shrs. Reda Pump	819.78
a) 2-9-53	
b) 100 shrs. McPhail Candy	46.95
a) 2-10-53	
b) 200 shrs. Lone Star Steel	1,920.40
a) 2-9-53	
b) 1 shr. Commonwealth Ed.	34.36
a) 1-22-54	
b) 100 shrs. Pickering Lumber	2,422.27
a) 6-16-54	
b) 100 shrs. Industrial Brownhoist	1,603.70
c) 200 shrs. Industrial Brownhoist	3,256.90
a) 6-8-55	
b) 200 shrs. Pickering Lumber	2,909.75
a) 9-16-57	
b) 15 shrs. Texas Ill. Nat. Gas	280.83
a) 9-16-57	

b) 15 shrs. Texas Ill. Nat. Gas	280.83
a) 9-16-57	
b) 100 shrs. Lyttons	626.05
a) 9-16-57	
b) 26 shrs. N. Ill. Gas	453.75
a) 9-16-57	
b) 100 shrs. Lyttons	626.05
a) 10-15-57	
b) 572 shrs. Livingston Oil	625.69
a) 9-16-57	
b) 15 shrs. Texas Ill. Natural Gas	280.83
a) 9-24-62	
b) 4 shrs. Commonwealth Edison	159.91
c) 100 shrs. Standard Oil of Indiana	4,377.72
d) 100 shrs. Standard Oil of Indiana	4,357.15
e) 15 shrs. Standard Oil of New Jersey	774.28
f) 9 shrs. Standard Oil of New Jersey	462.56
g) 100 shrs. AT&T	10,845.52
a) 8-30-51	
b) 160 shrs. Black Sevalls & Bryson	2,939.90
a) 7-26-50	
b) 250 shrs. Group Sec. Aviation	1,820.00
c) 60 shrs. Group Sec. Aviation	436.70
a) 7-27-50	
b) 100 shrs. Berkshire Fine Spinning	1,676.50
a) 9-26-60	
b) 200 shrs. Hartfield Stores	1,218.69
c) 6 shrs. Hartfield Stores	34.37
a) 10-23-52	
b) 50 shrs. Gerity Mich. Corp.	157.44
a) 2-10-53	
b) 200 shrs. Lone Star Steel	1,920.40
a) 2-9-53	
b) 175 shrs. Rothmoor Corp.	684.20

c) 1 shr. Commonwealth Edison	$ 34.36
a) 1-22-54	
b) 100 shrs. Pickering Lumber	2,422.27
a) 10-23-52	
b) 100 shrs. Gerity Mich. Corp.	326.79
a) 2-9-53	
b) 100 shrs. Reda Pump	819.78
a) 2-9-53	
b) 100 shrs. McPhail Candy	46.95
a) 12-22-52	
b) 200 shrs. Pickering Lumber	4,133.22
a) 6-8-55	
b) 200 shrs. Pickering Lumber	2,909.75
a) 9-24-62	
b) 100 shrs. Commonwealth Edison	4,120.03
c) 100 shrs. Commonwealth Edison	4,133.35

ANSWER OF L. STANBRIDGE MARTIN TO
INTERROGATORY 15
PURCHASE

a) 1-28-60	
b) $2,000.00 Ill. State Toll Hwy. Bonds	1,536.67

SALE

a) 2-16-65	
b) $2,000.00 Northern Ill. Toll Hwy. Bonds	2,025.83

24. State (a) the date, occasion, place, and nature of your first contact of any kind with Nay, (b) if different from the above, date, occasion, and place of your first personal meeting with Nay, and (c) when and how often thereafter you met personally with Nay up to and including June 1, 1968.

ANSWERS TO QUESTION 24:

Eugene Voita—(a) Do not remember. About 1944 some time. (c) same—about one a month.

Helen Feldkamp—a) and b) The exact date I do not remember, 1948 or '49 at the Federal Reserve Bank at the time of the conversion of the bonds. c) At First Securities perhaps three or four times; Mr. & Mrs. Nay visited me in 1953 for an overnight stay; the Nays gave a dinner party for me in October, 1967—we met at the home and dined at the Cliff Dwellers Club. Mr. & Mrs. Voita and Leon Carnovsky were present. This is my entire personal contact with Nay over the years.

Agnes Smith—I cannot remember. I saw Nay on business on several occasions at his office after my husband's death in 1948.

Anna Jesse—We met the Nays at the South Side apartment of Joseph Drake. See my husband's answer to this question.

William Jesse—a) My wife and I were invited to meet the Nays for tea by Joseph Drake at his apartment. This I think occurred in the autumn of 1936. This date is certainly correct within a year or two. (c) We met Mr. and Mrs. Nay from time to time at various social functions at the homes of friends on the South Side. The exact number is hard to estimate, but probably was less than a half dozen occasions per year.

Olga Hochfelder—My previous answers advised as to my first and subsequent meetings with Mr. Nay.

Helen Allison—I must have met Mr. Nay first in the late 1930's as the husband of Mrs. Nay with whom I worked in the League of Women Voters. When we moved to Blackstone Ave. in 1946, we would meet in

passing on the street and say "hello". We went to one dinner party at the Nay home—in early 1960's. In 1964 he rented a garage behind our apartment house and I would see him going or coming about once a week. I attended a big reception given by the Nays jointly with friends at the Quadrangle Club in 1967, I think. In early 1968 Mr. Nay and his wife came to see my new apartment.

Theresa Rothermel—(a) Mrs. Nay and I invited our husbands to lunch. Mostly by phone. 1st contact—business: I called him to invest in a certain stock.

Lurena Stubbs—Met him socially about 1942—saw him socially occasionally.

John M. Jackson—(a) My first meeting with Nay was in the late 1930's when my father introduced me to him. (b) My answer to (b) would be the same as my answer to (a) although the nature of the meeting was generally business—Nay was my father's investment advisor. (c) My meetings with Nay were very irregular because I lived during parts of the period from 1940 to 1968 in California, in Barrington, River Forest and Elmhurst, Illinois. I personally met with Nay many times during this 28 years and most meetings occurred in the offices of First Securities. Some of these meetings in the offices of the Company were brief because I would stop in to deliver or pick up a security sold or purchased for me by First Securities or to ask Nay some investment advice or information.

Elizabeth B. Jackson—My first meeting with Nay was probably in the early 1940's. I do not remember the occasion. I probably met him a dozen times during our lives.

Zearh A. Drake—I cannot remember when I first met Mr. Nay. It was shortly after my marriage to Joseph H. Drake, Jr. in 1943. I have not seen him since my husband's death in 1953.

Leon W. Carnovsky—I first met Nay about 1950 when my wife and I became members of a play reading group called the "Thirty Seven Players".

ANSWERS TO QUESTION 24:

Leon S. Martin—(a) 1941. Nay's office re investments. (b) Not applicable. (c) Seldom.

L. Stanbridge Martin—(a) About 1-21-60. (b) Not applicable. (c) Seldom.

SUPPLEMENTAL ANSWERS MADE AT THE REQUEST OF ERNST & ERNST TO QUESTION 24:

Theresa Rothermel—(a)After serving on a jury with Mrs. Nay in the late 1930s, Mrs. Nay and I invited our husbands to lunch. Thereafter we contacted each other mostly by phone. 1st contact on business was in the late 1930s. I called him to invest in a certain stock.

Lurena Stubbs—I cannot remember when I first met Nay, but I think I met him socially about 1942. I saw him socially occasionally thereafter.

Leon W. Carnovsky—I first met Nay about 1950 when my wife and I became members of a play reading group called the "Thirty Seven Players". I saw him six or eight times a year thereafter.

Olga Hochfelder—I first saw Nay in 1951 at his office. I was sent there by my employer Mr. Rothermel to receive investment advice from Nay.

SUPPLEMENTAL ANSWERS TO QUESTION 24 AT THE REQUEST OF ERNST & ERNST:

Leon S. Martin—(a) 1941. Nay's office re investments. (b) Not applicable. (c) Seldom. Perhaps 2 or 3 times.

L. Stanbridge Martin—(a) About 1-21-60 when I purchased through First Securities Company or Nay, Tollway Bonds. (b) Not applicable. (c) Seldom, perhaps two or three times altogether.

33. State (a) the date, place, occasion, and circumstances of your first discussion or meeting with Nay concerning your investment in the "fictitious and non-existent escrow" alleged in paragraph 4 of the Second Count of the First Amended Complaint, (b) whether you have knowledge of any witness to this occurrence or whether you have knowledge of any other person with any personal knowledge of such discussion or meeting, and, if so, state the full name and address of any such witness or person with personal knowledge.

JOINT AND SEVERAL ANSWER OF ALL RESPONDENTS TO QUESTION 33.

In response to your formal request for pertinent documents, all of this information was on December 15, 1971 furnished to you by us in great detail in the transcripts of our sworn testimony before Master Charles A. Bane in Case 68 C 1053 in this Court and in the many exhibits which we then produced and furnished you. Those transcripts and exhibits are hereby incorporated herein as our several answers to the foregoing Interrogatory.

Those exhibits are our business records of the transactions involved here and we hereby specify them as a sufficient answer to the above Interrogatory under Rule 33 (c) of the Rules of Civil Procedure for the United States District Courts.

ANSWERS TO QUESTION 33.

Leon S. Martin—(a) Before September, 1957. Either at 231 South La Salle or 134 South La Salle Street. (b) No.

L. Stanbridge Martin—(a) About February 16, 1965. (b) My parents.

SUPPLEMENTAL ANSWERS TO QUESTION 33 AT THE REQUEST OF ERNST & ERNST:

Leon S. Martin—(a) Before September, 1957. Either at 231 South La Salle or 134 South La Salle Street. First Securities Company had sold for us several stocks and bonds. Nay suggested that he could put the proceeds of these sales into an escrow at the Continental Bank which would yield 1% a month. (b) No.

L. Stanbridge Martin—(a) About February 16, 1965. Nay told my parents that one of the escrow investors had dropped out and asked them if their son would be interested in the escrow investment. Nay persuaded me to let First Securities Company sell my Illinois Tollway Bonds and invest the proceeds in the escrow. In addition he persuaded me to withdraw money that he knew I had at a low rate of interest in a Bank in Canada and invest it in the escrow.

ANSWER OF OLGA HOCHFELDER TO INTERROGATORY 33:

(a) In 1957, Nay called me by phone and asked me to come into his office. I did so, and at that time he told me of a "so-called escrow account" which he as President of First Securities had been given the opportunity to handle. He asked me if I would be interested in buying some of this "escrow account."

(b) None.

ANSWER OF AGNES SMITH TO INTERROGATORY 33:

(a) Nay called me in 1952 from his office at the First Securities Co. and asked me to come into his office. When I did so, he told me of an "escrow fund" his wife and daughter had invested in. Nay recommended that I sell my various stocks and invest in the "escrow fund," which I did.

(b) No.

ANSWER OF EUGENE VOITA TO INTERROGATORY 33:

(a) In the summer of 1949 Nay invited me and my wife to come into his office. At that time Nay explained that he and the First Securities Company had been employed by a loan company to set up an "escrow." He told us he would like to have us take a part in the "escrow."

(b) My wife, Mrs. Szada Voita, 5555 Sheridan Road, Chicago, Illinois.

ANSWER OF ANNA L. JESSE TO INTERROGATORY 33:

(a) On December 13, 1955, I was in Nay's office at the First Securities Co. when he told me the Company had done a great favor to a small investment company that loaned money at a high rate of interest. The money was maintained in an "escrow" which was paid for at a rate of 1% per month. Nay recomended that I invest in this "escrow."

(b) No.

ANSWER OF WILLIAM P. JESSE TO INTERROGATORY 33:

(a) My first discussion with Nay concerning the "escrow" took place around Thanksgiving, 1965, over the tele-

phone. Nay had sole our stocks for investment in the "escrow," and I was objecting that it was not a good thing to invest all in one company. Nay assured me the "escrow" was the safest thing he could recommend and urged me to put $22,000.00 into it. I took his advice.

(b) No.

ANSWER OF THERESA W. ROTHERMEL TO INTERROGATORY 33:

(a) Sometime around 1953, probably in Nay's office at First Securities, Nay told my husband and me about the "escrow." He said it was an investment opportunity we could make substantial interest on, was perfectly safe, and a good place to put our money. He said he couldn't reveal the name of the concern, but that it was a loan company whose board of directors he was on.

(b) No.

ANSWER OF HELEN C. ALLISON TO INTERROGATORY 33:

(a) Shortly before January 20, 1966, Nay called me on the telephone and asked if he could drop in at my apartment to tell me about some investment. He came over and talked to me about what later turned out to be the "fictitious and non-existent escrow."

(b) No knowledge of any witness to this occurrence.

ANSWER OF LURENA STUBBS TO INTERROGATORY 33:

(a) 1960 was the first time I personally discussed the "escrow" with Nay, although my husband had spoken with Nay about the escrow in 1954, and we had been investing our money in it since that time. I met with

Nay in his office at First Securities in 1960, and asked him about the advisability of investing in Sears, Roebuck Co. stock. Nay said we should not, as the stock market was overpriced and due for an adjustment, and we had the "escrow" account.

(b) No.

ANSWER OF JOHN M. JACKSON, INDIVIDUALLY AND AS TRUSTEE, TO INTERROGATORY #33:

My first discussion with Mr. Nay regarding the escrow was on Friday, August 31, 1962. It was at the offices of First Securities Company. Mr. Nay had telephoned me and suggested that my investment program needed some attention and that he would like me to come to his office to discuss my investments. I made an appointment for Friday, August 31, 1962, and went to the offices of First Securities Company and talked with Mr. Nay there. The conversation was in his office. So far as I can remember there was no one by Mr. Nay and me in the office during the conversation.

ANSWER OF ELIZABETH B. JACKSON TO INTERROGATORY #33:

I never discussed the escrow with Mr. Nay in a personal interview. My first discussion with him about the escrow was by telephone in October of 1963. So far as I know, no one was listening to that conversation.

CARNOVSKY INTERROGATORY 33(a):

(a) See the foregoing Interrogatory (26).

(b) I have no such knowledge.

DRAKE INTERROGATORY 33(a):

(a) Sometime after Joe and I were married in December 1942, I learned that Joe had made an investment in

the escrow. I cannot state the exact date, place or occasion or circumstance as this happened almost 30 years ago. See further Interrogatory 13 and the other interrogatories.

(b) No such knowledge.

ANSWER OF HELEN FELDKAMP TO QUESTION 33:

(a) In 1950, Nay told me over the telephone of an "escrow" he could give me the opportunity to invest in, as he was the financial advisor for a loan company. Nay said members of his family and close friends had given him money in "escrow" to loan to the loan companies.

(b) No.

41. Identify each document, if any, upon which you base your allegations in the Second Count of the First Amended Complaint that Nay "took no regular vacations."

ANSWERS OF ALL RESPONDENTS TO QUESTION 41:

We have no such documents. But that was common community knowledge known to his friends, offices associates and employees and stated by his wife and by him to their friends on many occasions.

ANSWERS TO QUESTION 41:

Leon S. Martin—We have no such document.

L. Stanbridge Martin—We have no such document.

42. State whether any person ever informed you that Nay took no regular vacations, and, if so, state with respect to each instance (a) the name and address of each such person so informing you, (b) the date when, the place where, and the circumstances in which such information was provided to you, (c) the names and addresses of all persons present when such information was provided to

you, and (d) the action, if any, taken by you as a result of receiving such information.

ANSWERS TO QUESTION 42:

Eugene Voita—No.

Helen Feldkamp—Living nearly 2000 miles from Chicago I had no opportunity to talk with others about Nay.

Agnes Smith—No. Nay's vacations were short and plans often changed or postponed.

Anna Jesse—No person ever informed me that Nay took "no regular vacations".

William Jesse—I do not know the name of any person that informed me as to Nay's vacation habit. I had the general impression that the vacations he took were very irregular.

Olga Hochfelder—I never asked as to whether or not Mr. Nay took a vacation.

Helen Allison—Mrs. Nay often complained that her husband would not take regular vacations. Plans would be made and cancelled. This was common knowledge amony her friends and acquaintances. She would tell me as we met for a chat on the street, or as we saw each other at a board meeting or lecture. Common friends would discuss it. This went on over years. (c) It is impossible for me to give these names. (d) I gave sympathy.

Theresa Rothermel—No.

Lurena Stubbs—No.

Zerah Drake—No.

John M. Jackson—No.

Elizabeth B. Jackson—No.

Leon W. Carnovsky—No.

ANSWERS TO QUESTION 42:

Leon S. Martin—No.

L. Stanbridge Martin—No.

44. Identify each document, if any, upon which you base your allegations in the Second Count of the First Amended Complaint that "the mail addressed to [First Securities] piled up unopened on [Nay's] desk" when Nay was absent from the office of First Securities.

ANSWER OF ALL REPONDENTS TO QUESTION 44:

Transcript previously furnished you at your request of testimony of Roy E. Campbell at pages 737-8 and 763-5.

JOINT ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 44:

Our counsel has previously furnished you at your request with a transcript of the testimony of Roy E. Campbell, office manager of First Securities Company of Chicago, who testified as above at pages 737-8 and 763-5.

50. State whether Nay ever took vacations from First Securities prior to June 1, 1968, and, if so, state the date and place of each such vacation.

ANSWERS TO QUESTION 50:

Eugene Voita—Not to my knowledge.

Helen Feldkamp—The only vacation I know about was in 1953 when Mrs. Nay spent a holiday in Arizona and Mr. Nay flew out to spend a weekend there and bring her home. On the way home they stayed overnight with me in Santa Fe.

Agnes Smith—Yes, he took short trips, but I had no reason or interest in the dates or places.

Anna Jesse—Mr. and Mrs. Nay did take a few irregular vacations, but I do not recall the year or time of year.

William Jesse—I do not know the particulars of any such vacations.

Olga Hochfelder—I would not know.

Helen Allison—I know of only one vacation, a short one,

Mr. Nay with his wife took. They drove through Finger Lake country of New York State and stayed for a few days at Lake Mohawk which Mrs. Nay and I knew from our Vassar College days. Mrs. Nay told me of this on the street. It was some time in the early 60's, I think.

Theresa Rothermel—Mr. & Mrs. Nay spent Christmas with her daughter.

Lurena Stubbs—Yes, but do not know times and places.

Zerah Drake—I do not know.

John M. Jackson—I have some recollection that Nay told me of some brief trips he had taken but I do not recall them specifically.

Elizabeth B. Jackson—My answer would be the same as my husband's.

Leon W. Carnovsky—I do not know.

ANSWERS TO QUESTION 50:

Leon S. Martin—My only knowledge is that Nay once sent me a postcard from England.

L. Stanbridge Martin—I have no knowledge.

57. Identify each document, if any, upon which you base your allegation that Ernst & Ernst did not inquire (a) whether the mail addressed to First Securities piled up unopened on Nay's desk when Nay was absent from the office of First Securities, or (b) whether Nay required that all mail addressed to him or to First Securities to his attention be opened only by him.

ANSWER OF ALL RESPONDENTS TO QUESTION 57:

We have previously in response to your request furnished you with the transcript of the testimony of Roy E. Campbell in which he testified at page 765:

"Q. Did you ever tell the representatives of Ernst & Ernst that no one but Nay was permitted to open mail addressed to the company in his attention?

A. No, I don't recall that I did.

Q. And did Ernst & Ernst ever ask you about the routine of restricting the opening of mail?

A. No, I do not believe they ever did.

Q. They never asked any question of you which would require the divulgence by you that you were under the restriction of not opening mail addressed to the company to the attention of Nay?

A. No, they did not."

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 57:

We have previously in response to your request furnished you with the transcript of the testimony of Roy E. Campbell in which he testified at page 765:

"Q. Did you ever tell the representatives of Ernst & Ernst that no one but Nay was permitted to open mail addressed to the company in his absence?

A. No, I don't recall that I did.

Q. And did Ernst & Ernst ever ask you about the routine of restricting the opening of mail?

A. No, I do not believe they ever did.

Q. They never asked any question of you which would require the divulgence by you that you were under the restriction of not opening mail addressed to the company to the attention of Nay?

A. No, they did not."

64. State whether any person ever informed you that a securities brokerage firm maintains inadequate internal controls if an officer of the firm requires that all mail addressed to him or to his attention be opened by him only and/or the said officer of the firm takes no regular vacations, and, if so, state with respect to each such

instance (a) the name and address of each such person so informing you, (b) the date when, the place where, and the circumstances in which such information was provided to you, (c) the names and addresses of all persons present when such information was provided to you, and (d) the action, if any, taken by you as a result of such information.

ANSWER OF ALL RESPONDENTS TO QUESTION 64:

Our counsel were informed in 1968 by Edward Byers Wilcox, former President of the American Institute of Certified Public Accountants, (See *Who's Who in America*) that it was inexcusable negligence for the auditor of a securities dealer to fail to discover these facts since such a securities dealer had no internal accounting control whatever under these facts.

Our counsel has since discussed the question with several Certified Public Accountants all of whom have confirmed Mr. Wilcox's statement.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 64:

Our counsel were informed in 1968 by Edward Byers Wilcox, former President of the American Institute of Certified Public Accountants, (See *Who's Who in America*) that it was inexcusable negligence for the auditor of a securities dealer to fail to discover these facts since such a securities dealer had no internal accounting control whatever under these facts.

Our counsel has since discussed the question with several Certified Public Accountants all of whom have confirmed Mr. Wilcox's statement.

SUPPLEMENTAL ANSWER TO QUESTION 64 BY ALL RESPONDENTS MADE AT THE REQUEST OF ERNST & ERNST

Edward Byers Wilcox died on February 13, 1972.

Our counsel were informed of the matters stated in our original answer by Leonard Spacek, C.P.A. (See *Who's Who in America*) of Arthur Andersen & Company, 69 West Washington Street, Chicago, Illinois on June 3, 1970 at the Museum of Science and Industry and on August 5, 1970 at the University Club of Chicago. The only persons present were Willard L. King and Leonard Spacek.

Our counsel were also informed of the matters stated in our original answer by Lloyd I. Coveney, C.P.A. and Richard L. Boerger, C.P.A., both of Arthur Andersen & Company, 69 West Washington Street, Chicago, Illinois, on December 8, 1970 at the office of King, Robin, Gale & Pillinger and the Attic Club. The only persons present were Mr. Coveney and Mr. Boerger and our counsel, Willard L. King and Stanley N. Gore.

65. If your allegation that a securities brokerage firm maintains inadequate or improper internal controls if an officer of the firm requires that all mail addressed to him or to his attention be opened only by him and/or the said officer of the firm takes no regular vacations is based upon any source other than as described or identified in your answers to the preceding two interrogatories, describe and identify fully each such other source.

ANSWER OF ALL RESPONDENTS TO QUESTION 65:

No other source.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 65:

No other source.

66. State whether you have knowledge from any source of any brokerage firm whose internal control rules (a) require that all mail addressed to an individual or to an individual's attention be opened by some person other than said individual or (b) require that some mail or a certain portion of mail addressed to an individual or to an individual's attention be opened by some person other than said individual.

ANSWER OF ALL RESPONDENTS TO QUESTION 66:

We have no such knowledge.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 66:

We have no such knowledge.

67. If your answer to the preceding interrogatory is in the affirmative, state and identify, as to each such brokerage firm, (a) its name and address and (b) the documents and persons or other sources from which you acquired such information.

ANSWER OF ALL RESPONDENTS TO QUESTION 67.

This question is not applicable.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 67:

This question is not applicable.

71. State whether you contend that Midwest, the Securities and Exchange Commission, the National Association of Securities Dealers, or any other entity would have taken any action with respect to First Securities and/or Nay if Ernst & Ernst had informed any such entity that improper or inadequate internal controls existed at First Securities by reason of the fact that Nay required that all mail be opened by him and that Nay took no vacations.

ANSWER OF ALL RESPONDENTS TO QUESTION 71.

Yes.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 71:

Yes.

72. If your answer to the preceding interrogatory is in the affirmative, state (a) the action that would have been taken by each such entity and (b) the documents or other information upon which you base your contention that such action would have been taken.

ANSWER OF ALL RESPONDENTS TO QUESTION 72:

We are not able to speculate in this way. Certainly these entities would have investigated if Ernst & Ernst had not been inescusably negligent in failing to report the existing dangerous conditions.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 72:

We are not able to speculate in this way. Certainly, these entities would have investigated if Ernst & Ernst had not been inexcusably negligent in failing to report the existing dangerous condition.

73. Describe each way in which Ernst & Ernst allegedly aided and abetted Nay in defrauding you other than its alleged failure to discover and report to Midwest that Nay required that all mail addressed to him or to his attention be opened only by him and that Nay took no regular vacations, including, as to each such way, (a) the date, manner, and circumstances in which Ernst & Ernst aided and abetted Nay, (b) the extent of your personal knowledge, and (c) any other source of your

information in this regard, including (i) the name and address of each informant, (ii) identification of each document providing such information, and (iii) the dates, places, witnesses, and circumstances of your obtaining such information.

ANSWER OF ALL RESPONDENTS TO QUESTION 73:

In failing to discover Nay's fraud or point out irregularities that would have led to its discovery, such as complete failure to comply with NASD Rule 27c and failure to report Nay's excessive borrowings from his Company.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 73:

In failing to discover Nay's fraud or point out irregularities that would have led to its discovery such as complete failure to comply with NASD Rule 27 (c) and failure to report Nay's excessive borrowing from his company.

ANSWERS OF ALL RESPONDENTS TO INTERROGATORY 73:

Ernst & Ernst aided and abetted Nay's fraud in certifying each year from 1960 to 1967 inclusive that First Securities Company was solvent when in fact it was not solvent.

Ernst & Ernst aided and abetted Nay's fraud by failing to note in its annual reports Nay's excessive borrowings from First Securities Company.

Ernst & Ernst aided and abetted Nay's fraud by failing to make any proper review of the internal accounting control of First Securities Company.

Ernst & Ernst aided and abetted Nay's fraud by failing to report that First Securities Company had not complied with NASD Rule 27 c.

Ernst & Ernst aided and abetted Nay's fraud by failing to report that the daily blotter of First Securities Com-

pany contained no record of correspondence relating to the purchase or sale of securities.

Ernst & Ernst aided and abetted Nay's fraud by failing to report that the capital of First Securities was far below the ratio of capital to indebtedness required by the rules of the Midwest Stock Exchange.

Ernst & Ernst aided and abetted Nay's fraud by failing to answer all of the questions on the questionnaire of the Midwest Stock Exchange.

Ernst & Ernst aided and abetted Nay's fraud by failing to discover Nay's thefts from the company, such as the Schueren thefts and the Moyer thefts.

Ernst & Ernst aided and abetted Nay's fraud by stating in its annual reports from 1960 to 1967 inclusive that its reports fairly stated the financial condition of First Securities Company.

Ernst & Ernst aided and abetted Nay's fraud by charging and accepting a fee each year from 1960 to 1967 inclusive for certifying to the Midwest Stock Exchange that First Securities Company was solvent when in fact it was insolvent.

Ernst & Ernst aided and abetted Nay's fraud by failing to instruct its auditors in charge of the audit of First Securities Company to ascertain whether the duties and responsibilities of the employees of First Securities Company were clearly defined and unmistakenably assigned in such ways that no single employee (a) had control of its entire operation or (b) had complete control over both transactions, documents and records controlling those transactions.

Ernst & Ernst aided and abetted Nay's fraud by failing to inspect all correspondence of the company relating to the purchase or sale of securities.

All of the above information was derived from the deposition of Ernst & Ernst's partner, J. M. Hooker,

and the Exhibits thereto attached, taken on August 24, 1971, a copy of which is attached.

74. State your opinion or belief as to the motive of Ernst & Ernst in allegedly aiding and abetting Nay to defraud you.

ANSWER OF ALL RESPONDENTS TO QUESTION 74.

We do not accuse Ernst & Ernst of deliberate, intentional fraud. With inexcusable negligence it took money for certifying a condition contrary to the facts and failing to report irregularities, known to it, or which should have been discovered by it, its report of which would have led to the discovery of Nay's fraud.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 74:

We do not accuse Ernst & Ernst of deliberate, intentional fraud. With inexcusable negligence it took money for certifying a condition contrary to the facts and failing to report irregularities, known to it, or which should have been discovered by it, its report of which would have led to the discovery of Nay's fraud.

75. Describe each alleged instance of a failure of Ernst & Ernst "to exercise proper or appropriate auditing procedures in making . . . audit[s] of First Securities" other than the alleged failure to discover alleged inadequate mail and vacation procedures of First Securities, including as to each instance (a) the date, manner, and circumstances in which Ernst & Ernst failed to exercise proper or appropriate auditing procedures, (b) the extent of your personal knowledge of such failure, and (c) any other source of your information in this regard, including (i) the name and address of each informant, (ii) identification of each document providing

such information, and (iii) the dates, places, witnesses, and circumstances of your obtaining such information.

ANSWER OF ALL RESPONDENTS TO QUESTION 75:

Failure at any time to discover Nay's fraud which should have been discovered by appropriate accounting procedures; failure at any time to report non-compliance with NASD Rule 27c; failure at any time to report Nay's excessive borrowing from his Company.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 75:

Failure at any time to discover Nay's fraud which should have been discovered by appropriate accounting procedures; failure at any time to report non-compliance with NASD Rule 27c; failure at any time to report Nay's excessive borrowing from his Company.

ANSWERS OF ALL RESPONDENTS TO INTERROGATORY 75:

This interrogatory has been completely answered in our answer to interrogatory 73.

79. State whether prior to June 1, 1968 you ever saw or obtained audit reports, financial statements, or other documents prepared by defendant Ernst & Ernst and relating to First Securities and/or Nay, and, if so, state with respect to each (a) the date and a description of each such audit report, financial statement, or other document, and (b) the source from which and date on which such audit report, financial statement, or other document was obtained.

ANSWER OF ALL RESPONDENTS TO QUESTION 79:

No.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 79:

No.

80. State how and in what manner you relied on the accuracy and completeness of surprise audit reports of First Securities by Ernst & Ernst to Midwest as alleged in paragraph 6 of the Second Count of the First Amended Complaint.

ANSWER OF ALL RESPONDENTS TO QUESTION 80:

We relied on Nay's membersip in the Midwest Stock Exchange which was based on these audit reports.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 80:

We relied on Nay's membership in the Midwest Stock Exchange which was based on these audit reports.

81. State the full name and address of any person connected with defendant Ernst & Ernst or defendant Midwest whom you knew or contacted prior to June 1, 1968 in connection with First Securities and/or Nay.

ANSWER OF ALL RESPONDENS TO QUESTION 81:

None.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 81:

None.

82. State whether you know of any partner, employee, or agent of Ernst & Ernst who, prior to June, 1968, knew of Nay's alleged fraud upon you.

ANSWER OF ALL RESPONDENTS TO QUESTION 82:

No.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 82:

No.

84. State whether you know of any partner, employee or agent of Ernst & Ernst who, prior to June, 1968, knew of any aspect of or any of the transactions constituting part of the alleged fraudulent conduct of Nay referred to in the Second Count of the First Amended Complaint.

ANSWER OF ALL RESPONDENTS TO QUESTION 84:

No.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 84:

No.

88. State whether you contend that you, Ernst & Ernst, Midwest, or the National Association of Securities Dealers would have discovered or known of or prevented the alleged fraud upon you by Nay if Ernst & Ernst had reported to Midwest that First Securities violated Rule 27(c) of the NASD and had inadequate or improper accounting controls because of Nay's alleged rule regarding the opening of mail and his alleged failure to take regular vacations.

ANSWER OF ALL RESPONDENTS TO QUESTION 88:

Yes.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 88:

Yes.

89. If your answer to the preceding interrogatory is in the affirmative, identfy and describe fully the basis for your answer, including a statement as to all action or inaction which would have occurred, the dates and the names and addresses of the persons or entities which would have taken or failed to take such action, and the source of your information.

ANSWER OF ALL RESPONDENTS TO QUESTION 89:

The basis of our answer is that the Midwest Stock Exchange, the SEC and the NASD would have investigated and discovered Nay's fraud if Ernst and Ernst had reported the irregularities aforesaid.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 89:

The basis of our answer is that the Midwest Stock Exchange, the SEC and the NASD would have investigated and discovered Nay's fraud if Ernst and Ernst had reported the irregularities aforesaid.

92. State whether you contend that defendant Ernst & Ernst (a) employed any device, scheme or artifice to defraud, (b) made any untrue statement of material fact or omitted to state a material fact necessary to make any statements made, in the light of the circumstances under which they were made, not misleading, or (c) engaged in any act, practice, or course of business which operated or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any

security, other than as stated in answer to any other interrogatory herein.

ANSWER OF ALL RESPONDENTS TO QUESTION 92:

We do not contend that Ernst & Ernst employed any scheme or artifice to defraud.

We do contend that Ernst & Ernst omitted to state material facts necessary to make any statement made in the light of the circumstances under which they were made not misleading when Ernst & Ernst certified every year that First Securities Company was solvent.

We do not contend that Ernst & Ernst intentionally engaged in any act, practice or course of business that operated as a fraud or deceit.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 92:

We do not contend that Ernst & Ernst employed any scheme or artifice to defraud.

We do contend that Ernst & Ernst omitted to state material facts necessary to make any statement made in the light of the circumstances under which they were made not misleading when Ernst & Ernst certified every year that First Securities Company was solvent.

We do not contend that Ernst & Ernst intentionally engaged in any act, practice or course of business that operated as a fraud or deceit.

97. State for each year during which your investment in the alleged "escrow" was in existence the full name and address of each person or entity who prepared or assisted in preparing your federal tax return.

Eugene Voita—None.

Helen Feldkamp—1951 David M. Lucas R.P.A.
Santa Fe, New Mexico
1953-66 W. C. Kneeland R.P.A.
Bishop Building
Santa Fe, New Mexico
1967 to present Raymond U. Jordan C.P.A.
P.O. Box 1386 until 1970 when he joined Neff & Company
Bishop Building Santa Fe

Agnes Smith—I prepared my own income tax return.

Anna Jesse—My husband assisted me in preparing our joint federal income tax return.

William Jesse—I prepared income tax forms myself for these years until 1968. For 1968 I had some help from Tofel, Forman & Co.

Olga Hochfelder—My income tax returns are made by my brother, Ernest Hochfelder.

Helen Allison—My tax return for 1966 was prepared by myself with Mr. Nay's help. For 1967, I made out the return which we then looked over and was corrected by Mr. Nay. The 1968 return was made out by Mr. Myron Goren, 8515 Avalon, Chicago, 60619.

Theresa Rothermel—Gale, Takahashi & Channon
110 So. Dearborn Street
Chicago

Lurena Stubbs—Mr. Milton Wright, 5550 Cornell Ave., Chicago

John M. Jackson—I prepared my own income tax return with no assistance.

Elizabeth B. Jackson—My husband prepared our joint income tax return.

Zerah A. Drake—John W. Donehoo, 1414 Barnett Bank Bldg., Jacksonville, Florida 32202

Leon Carnovsky—Rober Agron, 11 South La Salle Street, Chicago, Ill.

102. State whether you ever made inquiry to the Continental Illinois National Bank or any other financial institution prior to June 1, 1968 concerning the alleged "fictitious and non-existent escrow," and, if so, state (a) the full name and address of the institution to whom such communication was made, (b) the name of the individual or individuals at such institution to whom such communication was made, (c) the information obtained upon such inquiry, and (d) the action, if any, taken by you upon receipt of such information.

ANSWER OF ALL RESPONDENTS TO QUESTION 102:

No.

ANSWERS TO QUESTION 102:

Leon S. Martin—In May of 1968 my attorney, Charles Reimers, inquired at the Continental Bank and found that there was no escrow account and never had been.

L. Stanbridge Martin—No.

SUPPLEMENTARY ANSWER TO QUESTION 102 AT THE REQUEST OF ERNST & ERNST:

Leon S. Martin—In May of 1968 my attorney, Charles Reimers, inquired at the Continental Bank and found that there was no escrow account and never had been. Before that I had never made inquiry at the Continental Bank.

103. State whether you ever made inquiry to defendant Ernst & Ernst or to defendant Midwest concerning the financial condition of First Securities prior to June 1, 1968, and, if so, state (a) the full name and address of the person connected with defendant Ernst & Ernst or defendant Midwest to whom the inquiry was made and

the date of such inquiry, (b) the information obtained, and (c) the action, if any, taken by you upon receipt of such financial information.

ANSWER OF ALL RESPONDENTS TO QUESTION 103:

No.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 103:

No.

SUPPLEMENTAL ANSWERS MADE AT THE REQUEST OF ERNST & ERNST TO QUESTION 104:

Olga Hochfelder—I asked Mr. Nay about the escrow account and he stated at each time that if it were not 100% proper and honest, he would never have invested his wife's or daughter's money in the same. He never explained the escrow account any further than that.

JOHN M. JACKSON—The only inquiries I ever made concerning financial information relating to the escrow were of First Securities Company and Leston B. Nay and the only representative of First Securities Company to whom I addressed any such inquiry was Nay. The only information I ever obtained from such inquiry was, I now realize, glib generalities given so adroitly that I never did get specific information and the lack of it always seemed reasonable under the smooth flow of Nay's explanations. Nay told me that the funds were loaned to or invested with a small loan company; that the escrow was handled through a bank; that it was a very rare and advantageous investment made possible by the fact that First Securities Company had performed outstanding

services for the small loan company; that the investments were in large "Units" in which individual investors were permitted to participate; that the investment was safer than common stocks and somewhat better from a return standpoint than corporate bonds. The only action I took on the basis of this information, from time to time and prior to Nay's death, was to make additional investments in the escrow.

104. State whether you ever made inquiry to Nay, First Securities, or any other person or entity concerning financial information for the alleged "fictitious and non-existent escrow" and, if so, state (a) the full name and address of the person or entity to whom such communication was made and the date of such communication, (b) the information obtained upon such inquiry, and (c) the action, if any, taken by you upon receipt of such information.

ANSWERS TO QUESTION 104:

EUGENE VOLTA—No.

HELEN FELDKAMP—When I was first offered investment in the Escrow Fund Nay explained it to me as being 'short term unsecured loans to small loan companies, financed thru the Continental Illinois Bank.' This was a phone conversation and the date would be several days prior to July 15, 1950 which was the date of the first investment. The action I took was to continue to invest in the Escrow Fund over the next nine years.

AGNES SMITH—No. But see letter of Nay dated August 10, 1967, previously furnished you.

ANNA JESSE—I never asked Nay or anyone concerning financial information of "escrow".

WILLIAM JESSE—I made inquiries to Nay himself on two occasions over the telephone. I told him I was uneasy as to the financial stability of "escrow". He reassured me, said it was the safest investment he knew of and that I could withdraw my money invested at any time on two months' notice. He strongly advised me to delay withdrawing funds. I finally agreed to continue the investment a little longer.

OLGA HOCHFELDER—I asked Mr. Nay about the escrow account and he stated at each time that if it were not 100% proper and honest, he would never have invested his wife's or daughter's money in the same.

HELEN ALLISON—I made no inquiry to First Securities or to any person except Mr. Nay himself for financial information about the escrow. Soon after my first investment in the escrow I became uneasy because of the high interest being paid. He came to the house that afternoon and gave an explanation of how a loan company is built up. A short-term personal loan company is as near as I ever came to what was behind the escrow. That I did not completely understand at all, I took to be my ignorance of financial affairs. I accepted what he said and took no further action.

Theresa Rothermel—No.

LURENA STUBBS—No.

JOHN M. JACKSON—I made no such inquiries to Nay who explained that it was necessary to keep the investments in confidence to avoid pressure from other would be investors and because the loan com-

pany involved wished to keep the financing confidential.

ELIZABETH B. JACKSON—I made no such inquiries except to John M. Jackson who told me the facts stated in his answer to this question.

ZERAH A. DRAKE—No.

LEON W. CARNOVSKY—No.

JOINT AND SEVERAL ANSWER OF LEON S. MARTIN AND L. STANBRIDGE MARTIN TO QUESTION 104:

No.

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454; 71 C 1204) * *

MOTION FOR SUMMARY JUDGMENT

Defendant, Ernst & Ernst, by its attorneys in this regard, moves this court, pursuant to Rule 56 of the Federal Rules of Civil Procedure, as follows:

1. Defendant Ernst & Ernst requests the entry of summary judgment in favor of Ernst & Ernst as to the Second Count of the First Amended Complaint in Hochfelder, et al. v. Midwest Stock Exchange, et al. ("Hochfelder") and Martin, et al. v. Midwest Stock Exchange, et al. ("Martin") on the grounds that there is no genuine issue of material fact therein and that Ernst & Ernst is entitled to a judgment in both actions as a matter of law. Such motion is based upon (a) the pleadings in Hochfelder and Martin; (b) certain affidavits; (c) plaintiffs' answers to Ernst & Ernst's First Interrogatories, including all supplemental answers thereto; (d) the request of the Exchange in Martin for admission

of facts and genuineness of documents and plaintiffs' responses thereto; (e) the Order of this court entered October 3, 1972 granting summary judgment for the Exchange in Hochfelder and Martin.

2. In the alternative, if summary judgment is not granted for Ernst & Ernst upon the whole of the Second Count of the First Amended Complaint in both Hochfelder and Martin, Ernst & Ernst requests that this court ascertain what material facts are actually and in good faith uncontroverted, and that this court make an order specifying the facts that appear without substantial controversy in Hochfelder and/or Martin and the claims of the plaintiffs with respect to which summary judgment is granted and directing such further proceedings in the actions as the court may require.

3. The grounds of this motion are as follows:

A. Ernst & Ernst owed no duty to plaintiffs with respect to the escrow transactions, since, whatever may have been the duty undertaken by Ernst & Ernst as auditors of First Securities Company of Chicago ("First Securities"), that duty was to a class of persons (regular customers of First Securities) from which the escrow plaintiffs intentionally excluded themselves. Since Ernst & Ernst owed no duty to plaintiffs they cannot be liable to plaintiffs for any violation as alleged in the First Amended Complaint as a matter of law.

B. The second ground of Ernst & Ernst's motion is that, as a matter of law and as supported by the affidavits of certified public accountants associated with Ernst & Ernst and affidavits of certified public accountants independent of Ernst & Ernst, Ernst & Ernst audited First Securities in accordance with generally accepted auditing standards and cannot be liable for Nay's fraud upon the plaintiffs.

C. The third ground of the motion is that Ernst & Ernst had no duty to examine or to enforce compliance with Section 27(c) of the Rules of Fair Practice of the NASD, upon which plaintiffs' claims of negligence in both Hochfelder and Martin are based. In the absence of such a duty, plaintiffs' claims with respect to said Rules are without merit against Ernst & Ernst as a matter of law.

D. The fourth ground of Ernst & Ernst's motion is that its conduct, as a matter of law, could not have caused any damage to plaintiffs.

E. The fifth ground of the motion is that Ernst & Ernst, as a matter of law, could not be found to have aided and abetted Nay in his fraud because it had no knowledge thereof and did not participate in or affirmatively aid such fraud.

F. The sixth ground of the motion is that plaintiffs must be estopped from asserting any liability on the part of Ernst & Ernst because of their previous inconsistent conduct which included their failure to inform Ernst & Ernst of any aspect of the escrow transactions.

G. The seventh ground of the motion is that all of plaintiffs' claims are barred by the applicable three year statute of limitations.

Wherefore, defendant Ernst & Ernst prays for the entry of a summary judgment in its favor, with respect to the Second Count of the First Amended Complaints in Hochfelder and Martin.

Respectfully submitted,
Baker & McKenzie
By: /s/ Michael J. Madda
Attorneys for Defendant
Ernst & Ernst

700 Prudential Plaza
Chicago, Illinois 60601
312-828-0400

EXHIBIT A

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454 and 71 C 1204) * *

AFFIDAVIT OF ROY E. CAMPBELL

ROY E. CAMPBELL, duly sworn, on oath states as follows:

1. I have personal knowledge of the facts set forth below and would testify competently to such matters if called as a witness in this proceeding.

2. I am recently retired. I was employed until November, 1972 by John Nuveen & Co., 209 South LaSalle Street, Chicago, Illinois and was employed by that company continuously since 1968 when I left the employ of First Securities Company of Chicago ("First Securities") following the death of Leston B. Nay ("Nay") and the appointment of a Receiver for First Securities. John Nuveen & Co. is a broker and dealer in securities, and I was employed by securities brokerage firms continuously since 1924 except for a period during the Second World War when I was in the armed forces. My employment by First Securities began on February 25, 1946 and continued without interruption until after Nay's death in 1968. During the entire period of my employment by First Securities, I held the position of Cashier. I also held the position of Assistant Secretary and then the Secretary of First Securities. In about 1962 I was also designated Office Manager. During the entire period of my employment by First Securities, Nay was its President and my superior to whom I reported. I was also a director of First Securities for some years prior to the appointment of the Receiver, and I had purchased and owned 65 shares of the outstanding 1,950

shares of the common stock of First Securities at the time of Nay's suicide.

3. During the entire period of my employment by First Securities, I was in charge of and responsible for all of its books and records and accounting matters. At all times during my employment, I was fully familiar with all of the books and records of First Securities and supervised or performed all recording and accounting functions and other activities regarding such books and records. In addition, I was familiar with and supervised compliance with the record keeping and accounting rules and regulations of the National Association of Securities Dealers, Inc. (the "NASD"), the Midwest Stock Exchange (the "Exchange"), and the Securities and Exchange Commission (the "Commission") as they applied to First Securities.

4. Nay took vacations every year from 1946 until 1968. In addition, he was occasionally away from the office for long weekends. My best recollection is that Nay was away from the office for two or three weeks each year and that his vacation practices were similar to those of the other officers except that Nay may have taken vacations more frequently and for longer periods than did the other officers of First Securities. First Securities did not maintain records showing dates and times of vacations of its officers.

5. Although Nay, as President, exercised overall responsibility for business and financial affairs of First Securities, his only function with respect to the accounting or record keeping activities of First Securities was to approve and endorse confirmation tickets containing information relating to customers' transactions executed on the preceding day. Nay and one or two of the other officers would divide the tickets evenly among them, but no officer would approve or endorse a ticket with

respect to a transaction handled by himself. When Nay was on vacation, his part in this activity was assumed by one of the other officers of First Securities until Nay's return. Nay had no other duties with respect to the accounting or record keeping activities, and this was, therefore, the only duty of his which was assigned to other employees during the periods when Nay was absent from the office on vacations. There were never more than approximately 32 employees of First Securities, including Nay and myself and including approximately 20 salesmen. At the time of Nay's death, there were 10 salesmen and officers and 9 other employees, including Nay and myself.

6. Nay did not handle cash or securities at First Securities except in the few instances when a customer may have sent to him, as they would occasionally send to other salesmen, checks or securities for First Securities. In those instances, the checks and securities were walked over to the cashier's cage for handling. To my knowledge, neither Nay nor any other officer or employee of First Securities ever failed to deliver to the cashier's cage for deposit in First Securities' accounts checks drawn to the order of First Securities. I recall a few occasions when Nay and other salesmen received from customers checks drawn to them personally in connection with purchases for customers, but, to my knowledge, such funds were always delivered to the cage for deposit in the bank account of First Securities. In all instances where checks or securities were delivered to the cage on behalf of customers, a receipt of other acknowledgement was given or mailed to the customer from the cashier's cage.

7. The procedures with respect to incoming mail remained substantially the same during my entire employ-

ment at First Securities. Three or four persons were authorized to pick up the first mail of the day of First Securities at the Post Office, where their signatures were on file. As I recall, these persons were myself, Doris Ryan, Mary Alice Golik, and probably Nay. The balance of mail for the day was delivered by the regular postman. Mrs. Ryan performed secretarial functions for Nay and other employees, assisted me in my cashier duties, was a relief switchboard operator, and generally performed miscellaneous clerical work. Generally, Miss Golik, who was the switchboard operator, or Mrs. Ryan picked up the mail at the Post Office between 8:00 and 8:30 A.M. and brought it to the office. The mail would usually come in two bundles, one for envelopes and one for oversized items. After being brought to the office, the mail would be placed on a desk near the cashier's cage and would be sorted by the person who had picked it up with the assitance frequently of one or two other employees and occasionally with my assistance. Nay never picked up or sorted the mail. In sorting, the mail was divided between envelopes addressed to First Securities and envelopes marked to the attention of any individual employee. All mail in the latter category would be placed on the desk of the person whose name appeared on the envelope and that person would open the envelopes. In a few instances when an envelope with an individual's name on it contained checks or securities, that individual would bring the checks or securities to the cashier's cage.

8. Although all mail bearing an individual's name on it would be placed on the individual's desk to be opened by such individual, Nay was the only individual at First Securities who requested that no person other than himself open mail addressed to him personally or to his

attention. When Nay was out of town for vacation or for business reasons, he left instructions with Mrs. Ryan to hold all of his mail until he returned to the office. He would periodically call the office to inquire regarding the mail to him and occasionally would request that some or all of his unopened mail be forwarded to his residence for his review upon return to Chicago. Nay and the others employed at First Securities usually received a few pieces of mail each day with their names on the envelope, Nay perhaps a few more than the others. Although Nay was insistent that only he open his mail, I did not consider the fact that Nay imposed this rule to be of any particular significance in the office and thought it simply one of the many general office rules of First Securities.

9. I can recall only one instance during my twenty-two years of employment at First Securities when checks or securites were received in an envelope with Nay's name on it while he was away from the office. In that instance, securities which I had been expecting were received from a customer in Colorado in an envelope addressed to Nay's attention. I opened the envelope and recorded the receipt of the securities. Nay later complained strongly to me of the violation of the office rule.

10. In connection with all transactions in which securities were purchased by or through First Securities, regular confirmation of purchase forms were sent to each customer, accompanied by a business reply envelope preaddressed to First Securities. This was for the purpose of providing an envelope in which customers could forward their checks to First Securities postage free. Substantially all customers used the envelopes to forward their checks to First Securities. The envelopes bore no individual's name but only the name of First Securities.

The envelopes were not picked up by First Securities employees at the Post Office but were delivered directly to our office by a postman so that the postage due could be collected. The envelopes were delivered directly to the cashier's cage and were opened there. Upon receipt of checks in this manner, a receipt or acknowledgement was sent to the customer. Although I cannot recall specifically, to the best of my knowledge any plaintiffs in this proceeding who purchased securities through First Securities received and used such envelopes in connection with such transactions.

11. In addition to pre-addressed envelopes of First Securities and confirmation of purchase forms, First Securities maintained various printed forms which were utilized in the normal course of its securities business. In connection with every sale of a security by or through First Securities, a customer would receive a confirmation of sale form. In connection with the receipt for safekeeping of securities of a customer, the customer would sign and return to First Securities a printed safekeeping receipt form. Regular statements of accounts were sent to customers of First Securities pursuant to NASD and Commission rules and regulations. Other additional forms were used for more specialized transactions. To the best of my knowledge, any plaintiffs in this proceeding who purchased and sold securities by or through First Securities received all or some of such forms depending on the extent and nature of their securities transactions in the normal course of their brokerage accounts.

12. During the time of my employment, the books, records and office procedures of First Securities were examined by the Commission approximately 18 times, by the NASD approximately 15 times, and by the Ex-

change approximately 15 times. I understood that these examinations were part of the regular examination system and procedures of those entities, and in each instance the examinations resulted in approval of our systems and procedures. On two or three occasions, the Exchange brought representatives of newly admitted member companies to our office so that I could instruct these persons on our record keeping and the various systems designed to meet the Exchange's requirements. The procedures of First Securities with respect to correspondence of its salesmen, including Nay, were checked in the normal course of the above examinations, particularly in the examinations of the NASD, and at no time, to my knowledge did any representative of the Exchange, the NASD, or the Commission indicate that such procedures were inadequate and in no examination report of the Exchange, the NASD, or the Commission was any comment ever made concerning the inadequacy of such procedures. At no time did any representative of the Exchange, the NASD or the Commission ever inquire into the system maintained at First Securities with respect to the opening of mail. At each securities house at which I have worked, mail bearing an individual's name was or is opened by that individual without the requirment that a third party be present.

13. At no time prior to the death of Nay did I, nor, to my knowledge, did any other officer or employee of First Securities, have any knowledge that Nay obtained money personally from any of the persons now a plaintiff in these proceedings, that he issued receipts or other written documents relating to his obtaining such funds, that he was personally engaged in any transactions with the plaintiffs, nor did I or they, to my knowledge, have

any knowledge of the "escrow" alleged in this proceeding until after Nay's death.

/s/ Roy E. Campbell
Roy E. Campbell

Subscribed And Sworn
to before me this 6th
day of December, 1972.
/s/ Lorraine Kedzierski
Notary Public

EXHIBIT B

IN THE UNITED STATES DISTRICT COURT

• • (Caption—Nos. 71 C 454 and 71 C 1204) • •

AFFIDAVIT OF JERRY M. HOOKER

JERRY M. HOOKER, duly sworn, on oath states as follows:

1. I have personal knowledge of the facts set forth below and would testify competently to such facts if called as a witness in this proceeding.

2. I am a certified public accountant licensed by the State of Illinois and have been engaged in the full-time practice of accountancy with defendant, Ernst & Ernst, continuously since 1957, except for the period September 1959 to March 1960 when I was in the United States Army. Between 1957 and 1969 my positions with Ernst & Ernst were Assistant Accountant (1957-1959), Senior Accountant (1959-1963), Supervisor (1963-1966) and Manager (1966-1969). In 1969 I was admitted to partnership in Ernst & Ernst and have been a partner with that firm since then. My formal higher education includes four years at Northern Illinois University from which I received a Bachelor of Science degree in accounting

in 1958. I am and have been for a number of years a member of the American Institute of Certified Public Accountants and the Illinois Society of Certified Public Accountants. I am a member of the Section on Broker-Dealers of the Specialized Industries Committee of the Illinois Society of Certified Public Accountants. A substantial portion of my work with Ernst & Ernst consists of the audits of firms of securities brokers or dealers.

3. Ernst & Ernst audited the financial records and reported on the financial statements of First Securities Company of Chicago ("First Securities") annually from prior to 1946 until 1967. The last work performed by Ernst & Ernst for First Securities was with respect to a surprise audit of First Securties as of October 31, 1967. The work on that audit was completed and Ernst & Ernst's report delivered December 12, 1967. I participated in and have personal knowledge of the audits for each of the years 1957 through 1967 (except for the year 1959 when I was in the armed services). During the years I worked on the First Securities audits, I was and I remain familiar with the accounting methods and procedures and the system of internal control maintained by First Securities. In addition to having participated in said audits, I have reviewed and examined all records of Ernst & Ernst with respect to its audits of First Securities and have reviewed and examined all other records of Ernst & Ernst necessary to permit me to make, on my own knowledge, the statements hereinafter set forth.

4. Between 1957 and 1968, in addition to the audits of First Securities, I regularly participated in the audits of other firms of securities brokers or dealers engaged in the public securities business, four of such firms be-

ing members of the Midwest Stock Exchange. The generally accepted auditing and accounting standards and requirements, including those with respect to systems of internal control, which were in existence from prior to 1957 until 1968 with respect to brokers or dealers in the public securities business who were members of Midwest Stock Exchange, were largely derived from and expressed in the following: (a) Section 17 of the Securities Exchange Act of 1934 and Rule 17a-5 and Form X-17a-5 promulgated thereunder by the Securities and Exchange Commission ("SEC"), (b) Midwest Stock Exchange Financial Questionnaire and Instructions of the Midwest Stock Exchange ("Exchange") referred to in said Questionnaire, (c) "Audits of Brokers or Dealers in Securities" issued by the Committee on Auditing Procedure of the American Institute of Certified Public Accountants (1956), (d) "Auditing Standards and Procedures, Statements on Auditing Procedure No. 33" issued by the Committee on Auditing Procedure of the American Institute of Certified Public Accountants (1963), and (e) various other treatises and authorities on accounting and auditing procedures and standards. I am and was during my participation in the audits of First Securities fully familiar with the foregoing rules and authorities.

5. During the years 1957 through 1967, the audits of First Securities by Ernst & Ernst and its reports on the financial statements of First Securities were, in my opinion, made in accordance with generally accepted auditing standards and as prescribed by Rule 17A-5 and the other authorities referred to in the preceding paragraph and included a review of the accounting system of First Securities and its internal accounting control

and procedures for safeguarding securities in accordance with those authorities.

6. In my opinion, the accounting system and the internal accounting control and procedures for safeguarding securities of First Securities for the period from 1957 through 1967 contained no material inadequacies. I have read the affidavit of Roy E. Campbell dated December 6, 1972 and filed as Exhibit A in connection with Ernst & Ernst's Motion for Summary Judgment in this proceeding. The procedure described by Mr. Campbell in Exhibit A as existing at First Securities, permitting the President, Leston B. Nay ("Nay"), to open all mail addressed to him personally or to his attention, or prohibiting any person other than Nay from opening mail addressed to him personally or to his attention, or prohibiting any person other than Nay from opening such mail, did not constitute or result in a lack of internal accounting control at First Securities. All adequate systems of internal control of brokers or dealers in securities, including the system maintained at First Securities, contain numerous other procedures and measures to safeguard the firm's assets and to check the accuracy and reliability of its accounting data so that in no circumstances will the existence of a procedure with respect to mail, as described by Mr. Campbell, be relevant to or determinative of the existence or lack of internal accounting controls for any purposes, including for purposes of comments by auditors to regulatory bodies or national securities exchanges or for purposes of or in connection with an accountant's expression of an opinion on the financial statements of a broker or dealer in securities. With respect to the internal accounting control and procedures of the brokers or dealers in securities audited by the Chicago office of Ernst & Ernst dur-

ing 1957 through 1967, I did not know of any such client of Ernst & Ernst which prohibited its officers from opening mail addressed to them personally or to their attention.

7. The procedures followed by Ernst & Ernst in its audits of First Securities from 1957 through 1967 with respect to all customers' transactions included the testing of the recorded amounts on the ledger card maintained for each customer, on the daily blotters, and on other books and records of First Securities details of all transactions with or through First Securities, including those in which cash, checks to the order of First Securities, or securities were delivered to First Securities and checks drawn on an account of First Securities or securities were delivered by First Securities to customers or to their order. Details of each such securities transaction were recorded on a transaction statement of First Securities, and a confirmation copy of the transaction statement was mailed to the customer engaging in the transaction. The audit procedures followed by Ernst & Ernst in connection with its audit of First Securities, during all of the years of which I have knowledge, included a check and confirmation of the accuracy and implementation of these procedures of First Securities. Such checks and confirmations indicated that the system was adequately designed to provide all customers, including plaintiffs, appropriate confirmation statements from First Securities with respect to each securities transaction with or through First Securities.

8. Under generally accepted auditing standards, the primary audit procedure to determine the accuracy and correctness of the books and records of a broker or dealer in securities with respect to its customers' accounts is to request and obtain written confirmation from such customers with respect to such accounts. The Audit Requirements set forth in Form X-17A-5 provide that as of the audit date the independent public accountant shall perform the following:

"(6) Obtain written confirmations with respect to the following (see note):

• • •

"(f) Customers', partners', officers', directors', and respondent's accounts. Confirmation of these accounts may be in the form of a written acknowledgement of the accuracy of the statement of money balances, securities and/or commodities positions, and open contractual commitments (other than uncleared 'regular way' purchases and sales of securities) accompanying the first request for confirmation mailed by the independent public accountant. Customers' accounts without balances, position or commitments, and accounts closed since the last prior audit shall be confirmed on a test basis.

• • •

"Note: Compliance with requirements for obtaining written confirmation with respect to the above accounts shall be deemed to have been made if requests for confirmation have been mailed by the independent public accountant in an envelope bearing his own return address and second requests are similarly mailed to those not replying to the first requests, together with such auditing procedures as may be necessary; provided, however, that with respect to customers' accounts closed since the last prior audit the accountant may use either positive or negative confirmation requests;"

9. In connection with all Ernst & Ernst audits of First Securities between 1957 and 1967, all customers of First Securities, including plaintiffs, whose accounts reflected

long or short securities positions, cash positions other than zero, or open contractual commitments as of the annual audit date, were sent a request from First Securities, mailed by Ernst & Ernst, for a written confirmation to be made as to the accuracy of the statement of their accounts with First Securities. In each instance in which no response was made within aporoximately 15 days, a second request was sent by Ernst & Ernst to the customer who had failed to respond. For years prior to 1961, such requests for confirmation, as well as customer replies received by Ernst & Ernst, have been disposed of by Ernst & Ernst in its usual course of business prior to the commencement of these actions.

Attached hereto as Hooker Affidavit Exhibits A through L are photocopies of the responses of various plaintiffs to these confirmation requests during 1961 through 1967, as follows:

EXHIBIT	PLAINTIFF	DATE
A	Helen C. Allison	September 30, 1966
B	Olga Hochfelder	December 31, 1961
C	Olga Hochfelder	December 31, 1962
D	Olga Hochfelder	September 30, 1964
E	Olga Hochfelder	April 30, 1965
F	John M. Jackson, Trustee	December 31, 1961
G	John M. Jackson	December 31, 1961
H	John M. Jackson, Trustee	December 31, 1962
I	John M. Jackson	December 31, 1962
J	John M. Jackson and Elizabeth B. Jackson	December 31, 1962
K	Theresa W. Rothermel	December 31, 1961
L	Theresa W. Rothermel	October 31, 1967

None of the foregoing nor any other of the plaintiffs at any time ever informed Ernst & Ernst that their securities positions or account balances, or statements of open contractual commitments, which never reflected any transactions or positions with respect to said "escrow," were incorrectly reflected on the books and records of First Securities because their escrow investments were owed them by First Securities.

10. Under generally accepted auditing standards, one of the audit procedures to determine the existence of any unrecorded assets or liabilities of a broker or dealer in securities is to request and obtain a written statement from its proprietor or one of its officers with respect thereto. The Audit Requirements set forth in Form X-17A-5 provide that as of the audit date the independent public accountant shall:

> "(7) Obtain a written statement from the proprietor, partner (of a partnership) or officer (if a corporation) as to the assets, liabilities, and accountabilities, contingent or otherwise, not recorded on the books of the respondent."

In connection with all Ernst & Ernst audits of First Securities between 1957 and 1967, Ernst & Ernst obtained a written statement from Nay and Roy E. Campbell in compliance with the above quoted audit requirements and in compliance with generally accepted auditing standards. Attached to this Affidavit as Hooker Affidavit Exhibits M through T are photocopies of said statements with respect to the audit years 1960 through 1967. Similar written statements for prior years were disposed of by Ernst & Ernst in its usual couse of business prior to the commencement of these actions.

11. At no time did Ernst & Ernst prepare or examine the personal financial statements or tax returns of Nay

nor did Ernst & Ernst otherwise perform personal services for Nay individually. I did not, and, to my knowledge, no other partner or employee of Ernst & Ernst, ever had knowledge of Nay's financial condition, his obligations to any of the plaintiffs or of any transactions or dealings betwen Nay and any of the plaintiffs prior to Nay's death in June 1968.

12. At no time prior to Nay's death did I, nor, to my knowledge, did any other partner, employee or agent of Ernst & Ernst, have any knowledge of any escrow, fictitious and nonexistent or otherwise, described in the First Amended Complaint, or of any other escrow in which the plaintiffs invested or thought they were investing. nor did I, or, to my knowledge, did any other employee or agent of Ernst & Ernst, have knowledge, prior to Nay's death, that Nay had obtained funds from the plaintiffs, issued to the plaintiffs receipts, letters or other written instruments relating to the "escrow" or investments therein, or paid interest, reimbursed principal, disbursed funds, or otherwise had any transactions with the plaintiffs relating in any way to the alleged "escrow."

13. Neither I, nor, to my knowledge, was any other partner, employee or agent of Ernst & Ernst, ever contacted by any plaintiff requesting information regarding First Securities, Nay or the "escrow."

14. Prior to Nay's death I did not, nor, to my knowledge, did any other partner, employee or agent of Ernst & Ernst, have any knowledge of any of the correspondence between plaintiffs and Nay regarding the "escrow," or of the fraud alleged by plaintiffs or of any of the acts or omissions of Nay constituting a part of or relating to the alleged fraud upon the plaintiffs.

15. An examination by independent auditors to determine compliance with the rules and regulations of the National Association of Securities Dealers, Inc. ("NASD"), including its Rules of Fair Practice, is not and has never been within the scope of a regular annual audit of the financial condition of an NASD member by a certified public accountant. Neither the NASD, the SEC, nor any national securities exchange or any other authority requires the independent certified public accountants engaged in a regular annual audit of an NASD member to examine or report on compliance with the rules and regulations of the NASD, including its Rules of Fair Practice.

/s/ Jerry M. Hooker
Jerry M. Hooker

Subscribed And Sworn
to before me this 8th
day of December, 1972.
/s/ Barbara J. Gorski
Notary Public

EXHIBIT A

Helen C. Allison
5816 S. Blackstone Avenue
Chicago, Illinois 60637

FOR THE PURPOSE OF ASSISTING OUR AUDITORS IN MAKING THEIR REGULAR EXAMINATION OF OUR ACCOUNTS AT THE CLOSE OF BUSINESS SEP [illegible] WE WOULD APPRECIATE YOUR VERIFYING THE POSITION OF THE SECURITIES AND THE BALANCE IN YOUR ACCOUNT, AS SHOWN BELOW.

VERY TRULY YOURS,
[illegible]

SECURITIES LONG

NO SECURITY POSITION

THIS CONFIRMATION REQUEST DOES NOT INCLUDE PURCHASES AND SALES OF SECURITIES, IF ANY, DURING THE FOUR BUSINESS DAYS PRECEDING THE AUDIT DATE.

BALANCE { DEBIT -0-
CREDIT -0-

PLEASE SIGN THIS CONFIRMATION, NOTING DIFFERENCES IF ANY, AND MAIL IT DIRECTLY TO ERNST & ERNST, 231 SOUTH LA SALLE STREET, CHICAGO, ILLINOIS, 60604, IN THE ENCLOSED ENVELOPE. YOUR PROMPT COMPLIANCE WILL BE APPRECIATED AND WILL AVOID THE NECESSITY OF FURTHER CORRESPONDENCE.

THE ABOVE STATEMENT OF MY (OUR) ACCOUNT IS CORRECT.

SIGNED. Helen C. Allison

IMPORTANT NOTE
In the case of joint accounts, confirmations should be signed by both individuals. Confirmations signed by banks, corporations and partnerships should bear the name of the organization as well as the signature of authorized officer or partner. In the case of individuals, all confirmations should be signed by the person in whose name the account is carried. Acceptance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

NO. [illegible]

EXHIBIT B

[illegible]
Chicago, Illinois 60626

FOR THE PURPOSE OF ASSISTING OUR AUDITORS IN MAKING THEIR REGULAR EXAMINATION OF OUR ACCOUNTS AT THE CLOSE OF BUSINESS [illegible] WE WOULD APPRECIATE YOUR VERIFYING THE POSITION OF THE SECURITIES AND THE BALANCE IN YOUR ACCOUNT, AS SHOWN BELOW.

VERY TRULY YOURS,
[illegible]

SECURITIES LONG

50 sh. Eastern Mass. Street Ry Co. Adj. Stock

THE LONG SECURITIES SHOWN HEREON, IF ANY, INCLUDE THOSE HELD IN SAFEKEEPING

BALANCE { DEBIT -0-
CREDIT -0-

PLEASE SIGN THIS CONFIRMATION, NOTING DIFFERENCES IF ANY, AND MAIL IT DIRECTLY TO ERNST & ERNST, 231 SOUTH LA SALLE STREET, CHICAGO, ILLINOIS, 60604, IN THE ENCLOSED ENVELOPE. YOUR PROMPT COMPLIANCE WILL BE APPRECIATED AND WILL AVOID THE NECESSITY OF FURTHER CORRESPONDENCE.

THE ABOVE STATEMENT OF MY (OUR) ACCOUNT IS CORRECT.

SIGNED. Olga Horlander

IMPORTANT NOTE
In the case of joint accounts, confirmations should be signed by both individuals. Confirmations signed by banks, corporations and partnerships should bear the name of the organization as well as the signature of authorized officer or partner. In the case of individuals, all confirmations should be signed by the person in whose name the account is carried. Acceptance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

NO. [illegible]

BEST COPY AVAILABLE

EXHIBIT C

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No. C 20

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS DEC 24 1959

IS CORRECT. (SIGNED) Olga Hochfelder

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Compliance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

EXHIBIT D

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No.

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS

IS CORRECT. (SIGNED) Olga Hochfelder

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Compliance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

EXHIBIT F

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No. 93

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS Dec 31 1951

IS CORRECT. (SIGNED) John D. Jackson Jr. Treasurer

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Compliance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

EXHIBIT E

ALERT CONFIRMATION

Olga Clara Hochfelder
6429 N. Sheridan Road
Chicago, Illinois 60626

FOR THE PURPOSE OF ASSISTING OUR AUDITORS IN MAKING THEIR REGULAR EXAMINATION OF OUR ACCOUNTS AT THE CLOSE OF BUSINESS DEC 24 1959 WE WOULD APPRECIATE YOUR VERIFYING THE POSITION OF THE SECURITIES AND THE BALANCE IN YOUR ACCOUNT, AS SHOWN BELOW.

VERY TRULY YOURS,

FIRST SECURITIES CO OF CHICAGO
231 S LA SALLE STREET
CHICAGO, ILLINOIS

SECURITIES LONG

50 shs. Eastern Mass.Street Ry.Co.Adj.Stock
75 " Vapor Corporation
50 " Kratter Corp.

THE LONG SECURITIES SHOWN HEREON, IF ANY, INCLUDE THOSE HELD IN SAFEKEEPING

THIS CONFIRMATION REQUEST DOES NOT INCLUDE PURCHASES AND SALES OF SECURITIES, IF ANY, DURING THE FOUR BUSINESS DAYS PRECEDING THE AUDIT DATE.

BALANCE { DEBIT 0 / CREDIT 0

PLEASE SIGN THIS CONFIRMATION, NOTING DIFFERENCES IF ANY, AND MAIL IT DIRECTLY TO ERNST & ERNST, 231 SOUTH LA SALLE STREET, CHICAGO, ILLINOIS, 60604, IN THE ENCLOSED ENVELOPE. YOUR PROMPT COMPLIANCE WILL BE APPRECIATED AND WILL AVOID THE NECESSITY OF FURTHER CORRESPONDENCE.

THE ABOVE STATEMENT OF MY (OUR) ACCOUNT IS CORRECT.

SIGNED Olga Hochfelder

IMPORTANT NOTE
In the case of joint accounts, confirmations should be signed by both individuals. Confirmations signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all confirmations should be signed by the persons in whose name the account is carried. Compliance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

NO. C 20 1

BEST COPY AVAILABLE

EXHIBIT G

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No. 92

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS DEC 31 1951

IS CORRECT. (SIGNED) John M. Jackson

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Observance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

EXHIBIT H

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No.

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS DEC 31 1951

IS CORRECT. (SIGNED) John M. Jackson Dec'd

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Observance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

EXHIBIT I

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No. C3

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS DEC 31 1951

IS CORRECT. (SIGNED) John M. Jackson

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Observance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

EXHIBIT J

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No.

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS DEC 31 1952

IS CORRECT. (SIGNED) John M. Jackson Dec'd

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Observance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

EXHIBIT K

ERNST & ERNST
231 SO. LA SALLE STREET
CHICAGO 4, ILL.

No. 187

THE STATEMENT OF MY ACCOUNT WITH

FIRST SECURITIES COMPANY
OF CHICAGO

AT THE CLOSE OF BUSINESS DEC 31 1951

IS CORRECT. (SIGNED) Theresa H. Rothermel

IF THE ENCLOSED STATEMENT IS NOT CORRECT, KINDLY INDICATE EXCEPTIONS ON REVERSE SIDE OF THIS CARD.

In the case of joint accounts, cards should be signed by both individuals. Cards signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all cards should be signed by the person in whose name the account is carried. Observance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

BEST COPY AVAILABLE

EXHIBIT L

ASSET CONFIRMATION

[redacted]

FOR THE PURPOSE OF ASSISTING OUR AUDITORS IN MAKING THEIR REGULAR EXAMINATION OF OUR ACCOUNTS AT THE CLOSE OF BUSINESS October 31, 19[illegible] WE WOULD APPRECIATE YOUR VERIFYING THE POSITION OF THE SECURITIES AND THE BALANCE IN YOUR ACCOUNT, AS SHOWN BELOW.

VERY TRULY YOURS,

FIRST SECURITIES COMPANY OF CHICAGO

SECURITIES LONG

100 U.S. Treasury Bills 1/11/68

THIS CONFIRMATION REQUEST DOES NOT INCLUDE PURCHASES AND SALES OF SECURITIES, IF ANY, DURING THE FOUR BUSINESS DAYS PRECEDING THE AUDIT DATE.

THE LONG SECURITIES SHOWN HEREON, IF ANY, INCLUDE THOSE HELD IN SAFEKEEPING

CUSTOMERS' CREDIT BALANCES ARE PROPERLY ACCOUNTED FOR ON OUR BOOKS, ARE NOT SEGREGATED, MAY BE USED IN THE OPERATION OF THIS FIRM'S BUSINESS AND ARE PAYABLE UPON DEMAND.

BALANCE { DEBIT ____ / CREDIT $101.91

PLEASE SIGN THIS CONFIRMATION, NOTING DIFFERENCES IF ANY, AND MAIL IT DIRECTLY TO ERNST & ERNST, 231 SOUTH LA SALLE STREET, CHICAGO, ILLINOIS, 60604, IN THE ENCLOSED ENVELOPE. YOUR PROMPT COMPLIANCE WILL BE APPRECIATED AND WILL AVOID THE NECESSITY OF FURTHER CORRESPONDENCE.

THE ABOVE STATEMENT OF MY (OUR) ACCOUNT IS CORRECT.

SIGNED Theresa W. Rothermel

IMPORTANT NOTE
In the case of joint accounts, confirmations should be signed by both individuals. Confirmations signed by banks, corporations and partnerships should bear the name of the institution as well as the signature of authorized officer or partner. In the case of individuals, all confirmations should be signed by the person in whose name the account is carried. Compliance of the above conditions will eliminate the necessity of further correspondence on account of incorrect signatures.

NO.

Exhibit M

FIRST SECURITIES COMPANY OF CHICAGO

134 SOUTH LA SALLE STREET
CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANdover 3-1200
TELETYPE CG—1200

January 12, 1960

Ernst and Ernst
231 South La Salle Street
Chicago 4, Illinois

Gentlemen:

The following representations are made to you incident to your examination of the statement of financial condition of First Securities Company of Chicago as at the close of business December 31, 1959 and of its statements of earnings and retained earnings for the year then ended, such representations as to the matters referred to being true, or fair estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at December 31, 1959 are valid receivables and payables.

The company had no contractual commitments and no material contingent or other possible liabilities.

The specimen copy of the 6 1/2% Cumulative Twelve-Year Income Debentures, due December 15, 1966, delivered to you, is an authentic copy of the issued Debentures. At December 31, 1959, the total principal amount of the Debentures outstanding was:

6 1/2% Income Debentures, due December 15, 1966 $35,000.00.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between January 1, 1959 and December 31, 1959.

No events have occurred and no facts have been discovered since December 31, 1959, which would make the statement of financial condition as of that date, or the statements of earnings and retained earnings for the year then ended materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge, there is nothing reflecting upon the honesty of members of our organization.

-2-

Ernst and Ernst January 12, 1960

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed appropriate for the purpose of expressing an opinion on the financial statements, and that such tests would not necessarily disclose all irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

President

Secretary

dr

EXHIBIT N

FIRST SECURITIES COMPANY OF CHICAGO
134 SOUTH LA SALLE STREET
CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANdover 3-1830
TELETYPE CG—1809

January 12, 1962

Ernst and Ernst
231 South La Salle Street
Chicago 4, Illinois

Gentlemen:

The following representations are made to you incident to your examination of the statement of financial condition of First Securities Company of Chicago as at the close of business December 31, 1961 and of its statements of income and retained earnings for the year then ended, such representations as to the matters referred to being true, or fair estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at December 31, 1961 are valid receivables and payable, but do not include regular way trades between December 22, 1961 and December 31, 1961.

The Company had no contractual commitments and no material contingent or other possible liabilities.

The specimen copy of the 6 1/2% Cumulative Twelve-Year Income Debentures, due December 15, 1966, delivered to you, is an authentic copy of the issued Debentures. At December 31, 1961, the total principal amount of the Debentures outstanding was:

6 1/2% Income Debentures, due December 15, 1966 $25,500.00.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between January 1, 1961 and January 11, 1962.

No events have occurred and no facts have been discovered since December 31, 1961 which would make the statement of financial condition as of that date, or the statements of income and retained earnings for the year then ended materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge, there is nothing reflecting upon the honesty of members of our organization.

January 12, 1962

Ernst and Ernst

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed appropriate for the purpose of expressing an opinion on the financial statements, and that such tests would not necessarily disclose irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

President

Secretary

dr

EXHIBIT O

FIRST SECURITIES COMPANY OF CHICAGO
134 SOUTH LA SALLE STREET
CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANdover 3-1820
TELETYPE CG—1399

January 11, 1963

Ernst and Ernst
231 South La Salle Street
Chicago 4, Illinois

Gentlemen:

The following representations are made to you incident to your examination of the statement of financial condition of First Securities Company of Chicago as at the close of business December 31, 1962 and of its statements of income and retained earnings for the year then ended, such representations as to the matters referred to being true, or their estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at December 31, 1962 are valid receivables and payable, but do not include regular way trades between December 26, 1962 and December 31, 1962.

The Company had no contractual commitments and no material contingent or other possible liabilities.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between January 1, 1961 and January 11, 1963.

No events have occurred and no facts have been discovered since December 31, 1962 which would make the statement of financial condition as of that date, or the statements of income and retained earnings for the year then ended materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge, there is nothing reflecting upon the honesty of members of our organization.

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

-2-

January 11, 1963

Ernst and Ernst

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed apropriate for the purpose of expressing an opinion on the financial statements, and that such tests would not necessarily disclose irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

President

Secretary

dr

EXHIBIT P

Exam 9/11/63

FIRST SECURITIES COMPANY OF CHICAGO

134 SOUTH LA SALLE STREET

CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANdover 3-1330
TELETYPE CG—1330

September 13, 1963

Hooker

Ernst and Ernst
231 South La Salle Street
Chicago 4, Illinois

Gentlemen:

The following representations are make to you incident to you examination of Answers to Financial Questionnaire of First Securities Company of Chicago as at the close of business August 30, 1963, such representations as to the matters referred to being true, or fair estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at August 30, 1963, are valid receivables and payables.

Following is a complete summary of the Company's net unsold contractual commitments that were not recorded in a ledger account for money as of August 30, 1963, other than uncleared regular way purchases and sales of securities made August 27, 1963 to August 30, 1963 inclusive:

	Liability of August 30, 1963	
	Number of Shares	Amount
Eastern Investors, Incorporated Class "A" Preference Stock	2500	$9,250.00

The 2500 Shares were sold subsequent to August 30, 1963.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between January 1, 1963 and September 13, 1963.

September 13, 1963

Ernst and Ernst

No events have occurred and no facts have been discovered since August 30, 1963 which would make the Answers to Financial Questionnaire as of the date, materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge, there is nothing reflecting upon the honesty of members of our organization.

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed appropriate for the purpose of expressing an opinion on the Answers to Financial Questionnaire, and that such tests would not necessarily disclose irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

(Illegible)
President

(Illegible)
Secretary

mac

EXHIBIT Q

FIRST SECURITIES COMPANY OF CHICAGO
134 SOUTH LA SALLE STREET
CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANdover 3-1530
TELETYPE 312-222-0834

October 9, 1964

Ernst and Ernst
231 South La Salle Street
Chicago, Illinois 60604

Gentlemen:

The following representations are made to you incident to your examination of Answers to Financial Questionnaire and the Statement of Financial Condition of First Securities Company of Chicago as at the close of business September 30, 1964, such representations as to the matters referred to being true, or fair estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at September 30, 1964, are valid receivables and payable, but do not include regular way trades between September 25, 1964 and September 30, 1964.

The Company had no contractual commitments and no material contingent or other possible liabilities as of September 30, 1964.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between September 13, 1963 and October 9, 1964.

No events have occurred and no facts have been discovered since September 30, 1964 which would make the Answers to Financial Questionnaire and the Statement of Financial Condition as of the date, materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge there is nothing reflecting upon the honesty of members of our organization.

October 9, 1964

Ernst and Ernst

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed appropriate for the purpose of expressing an opinion on the Answers to Financial Questionnaire and the Statement of Financial Condition, and that such tests would not necessarily disclose irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

President

Secretary

dr

EXHIBIT R

FIRST SECURITIES COMPANY OF CHICAGO
134 SOUTH LA SALLE STREET
CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANdover 3-1320
TELETYPE 312-922-0624

May 17, 1965

Ernst and Ernst
231 South La Salle Street
Chicago, Illinois 60604

Gentlemen:

The following representations are made to you incident to your examination of Answers to Financial Questionnaire and the Statement of Financial Condition of First Securities Company of Chicago as at the close of business April 30, 1965, such representations as to the matters referred to being true, or fair estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at April 30, 1965, are valid receivables and payables, but do not include regular way trades between April 27, 1965 and April 30, 1965.

The Company had no contractual commitments and no material contingent or other possible liabilities as of April 30, 1965.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between October 9, 1964 and May 17, 1965.

No events have occurred and no facts have been discovered since April 30, 1965 which would make the Answers to Financial Questionnaire and the Statement of Financial Condition as of the date, materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge there is nothing reflecting upon the honesty of members of our organization.

BEST COPY AVAILABLE

Ernst and Ernst May 17, 1965

No options to purchase securities of the Company were granted except as noted in Note A to the Answers to Financial Questionnaire and the Statement of Financial Condition.

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed appropriate for the purpose of expressing an opinion on the Answers to Financial Questionnaire and the Statement of Financial Condition, and that such tests would not necessarily disclose irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

L. [illegible] B. Nay
President

R. E. Campbell
Secretary

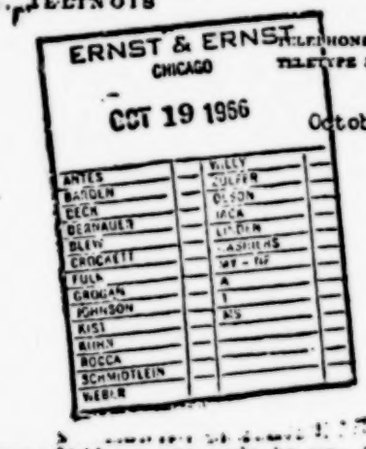
dr

EXHIBIT S

FIRST SECURITIES COMPANY OF CHICAGO
134 SOUTH LA SALLE STREET
CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANDover 3-1320
TELETYPE 312-222-0834



October 17, 1966

Low value

Ernst and Ernst
231 South LaSalle Street
Chicago, Illinois 60604

Gentlemen:

The following representations are made to you incident to your examination of Answers to Financial Questionnaire and the Statement of Financial Condition of First Securities Company of Chicago as at the close of business September 30, 1966, such representations as to the matters referred to being true, or fair estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at September 30, 1966, are valid receivables and payables, but do not include regular way trades between September 27, 1966 and September 30, 1966.

The Company had no contractual commitments and no material contingent or other possible liabilities as of September 30, 1966.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between May 17, 1965 and October 17, 1966.

No events have occurred and no facts have been discovered since September 30, 1966 which would make the Answers to Financial Questionnaire and the Statement of Financial Condition as of the date, materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge there is nothing reflecting upon the honesty of members of our organization.

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

BEST COPY AVAILABLE

Ernst and Ernst October 17, 1966

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed appropriate for the purpose of expressing an opinion on the Answers to Financial Questionnaire and the Statement of Financial Condition, and that such tests would not necessarily disclose irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

President

Secretary

dw

EXHIBIT T

FIRST SECURITIES COMPANY OF CHICAGO
134 SOUTH LA SALLE STREET
CHICAGO, ILLINOIS 60603

MEMBER
MIDWEST STOCK EXCHANGE

TELEPHONE ANdover 3-1320

November 22, 1967

Ernst and Ernst
231 South LaSalle Street
Chicago, Illinois 60604

Gentlemen:

The following representations are made to you incident to your examination of Answers to Financial Questionnaire and the Statement of Financial Condition of First Securities Company of Chicago as at close of business October 31, 1967, such representations as to the matters referred to being true, or fair estimates to the best of our knowledge and belief.

Debit and credit balances with customers, brokers and dealers as reflected in our books at October 31, 1967 are valid receivables and payables, but do not include regular way trades between October 27, 1967 and October 31, 1967.

The Company had no contractual commitments and no material contingent or other possible liabilities as of October 31, 1967.

Minutes of meetings of stockholders and directors as exhibited to you are complete and authentic records of such meetings held between August 30, 1966 and November 22, 1967.

No events have occurred and no facts have been discovered since October 31, 1967 which would make the Answers to Financial Questionnaire and the Statement of Financial Condition as of the date, materially inaccurate or misleading. No shortages or irregularities have been discovered, either already closed or now in abeyance, that have not been disclosed to you; and to our knowledge there is nothing reflecting upon the honesty of members of our organization.

To our knowledge, no charges are pending against the Company for alleged violations of Federal, State or local laws.

-2-

Ernst and Ernst

November 22, 1967

We understand that you have examined or tested accounting records of the Company and other supporting evidence by methods and to the extent you deemed appropriate for the purpose of expressing an opinion on the Answers to Financial Questionnaire and the Statement of Financial Condition, and that such tests would not necessarily disclose irregularities should any exist.

Very truly yours,

FIRST SECURITIES COMPANY OF CHICAGO

L. B. Nay
President

R. E. Campbell
Secretary

dr

EXHIBIT C

IN THE UNITED STATES DISTRICT COURT

• • (Caption—Nos. 71 C 454 and 71 C 1204) • •

AFFIDAVIT OF NEWELL P. CROCKETT

NEWELL P. CROCKETT, duly sworn, on oath states as follows:

1. I have personal knowledge of the facts set forth below and would testify competently to such facts if called as a witness in this proceeding.

2. I am a certified public accountant licensed by the State of Illinois and have been engaged in the full time practice of accountancy in the Chicago office of defendant Ernst & Ernst continuously since 1946. Between 1946 and 1961, my positions with Ernst & Ernst were Assistant Accountant (1946-1947), Senior Accountant (1947-1949), Supervisor (1949-1956), and Manager (1956-1961). In 1961, I was admitted to partnership in Ernst & Ernst and have been a partner wtih that firm since then.

3. Ernst & Ernst audited the financial records and reported on the financial statements of First Securities Company of Chicago ("First Securities") annually from prior to 1946 until 1967. During the years 1952 through 1957, I was Supervisor or Manager in charge of the First Securities audits, and have personal knowledge of all auditing procedures followed by Ernst & Ernst in such audits. During such years, I was fully familiar with the books and records, accounting methods and procedures, and the systems of internal control maintained by First Securities, and, in connection with such audits, I dealt with Leston B. Nay and Roy E. Campbell, President and Cashier respectively of First Securities.

4. All customers of First Securities whose accounts reflected long or short securities positions, cash positions other than zero, or open contractual commitments as of the annual audit date received a request from First Securities, initiated by Ernst & Ernst, for a written confirmation to be made directly to Ernst & Ernst as to the accuracy of the statements of their acounts with First Securities. All such confirmation requests and the responses to them for audits during the years 1952 through 1957 have subsequently been disposed of in the usual course of business by Ernst & Ernst. No customers at any time ever informed Ernst & Ernst that their securities positions, account balances, or statements of open contractual commitments, were incorrect because they did not reflect transactions or positions with respect to the alleged "escrow" or that any amount of "escrow" investments were owed to them by First Securities.

5. At no time did Ernst & Ernst prepare or examine the personal financial statements or tax returns of Leston B. Nay ("Nay") nor did Ernst & Ernst otherwise perform personal services for Nay individually. I did not have, nor to my knowledge, no other partner, employee or agent of Ernst & Ernst ever had, knowledge of Nay's financial position or his obligations to any of the plaintiffs, or of any transactions or dealings between Nay and any of the plaintiffs prior to Nay's death in June 1968.

6. At no time prior to Nay's death did I, nor, to my knowledge, did any other partner, employee or agent of Ernst & Ernst, have any knowledge of any escrow, fictitious or nonexistent or otherwise, as described in the proceedings herein, or of any other escrow in which the plaintiffs invested or thought they were investing nor did I, nor, to my knowledge, did any other partner, employee or agent of Ernst & Ernst, have any knowledge,

prior to Nay's death, that Nay had obtained funds from the plainitffs, had issued to the plaintiffs receipts, letters, or other written instruments relating to the "escrow" or investments therein, or had paid interest, reimbursed principal, disbursed funds, or otherwise had any transactions with the plaintiffs relating in any way to the alleged "escrow."

7. I was not, nor, to my knowledge, was any other partner, employee, or agent of Ernst & Ernst, ever contacted by any plaintiff requesting information regarding the "escrow."

8. Prior to Nay's death, I did not, nor, to my knowledge, did any other partner, employee, or agent of Ernst & Ernst, have any knowledge of any of the correspondence between plaintiffs and Nay regarding the "escrow," or the fraud alleged by plaintiffs, or any of the acts or omissions of Nay constituting a part of or relating to the alleged fraud upon the plaintiffs.

Further affiant sayeth not.

/s/ Newell P. Crockett
Newell P. Crockett

Subscribed and sworn to
before me this 11th
day of December, 1972.
/s/ Barbara J. Gorski
Notary Public

EXHIBIT D

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454 and 71 C 1204) * *

AFFIDAVIT OF LEROY E. KIST

LEROY E. KIST, duly sworn, on oath states as follows:

1. I have personal knowledge of the facts set forth below and would testify competently to such facts if called as a witness in this proceeding.

2. I am a certified public accountant licensed by the State of Illinois and have been engaged in the full time practice of accountancy in the Chicago office of defendant Ernst & Ernst continously since 1941. Between 1941 and 1961, my positions with Ernst & Ernst were Assistant Accountant (1941-1944), Senior Accountant (1944-1948), Supervisor (1948-1955), and Manager (1955-1961). In 1961, I was admitted to partnership in Ernst & Ernst and have been a partner with that firm since then.

3. Ernst & Ernst audited the financial records and reported on the financial statements of First Securities Company of Chicago ("First Securities") annually from prior to 1946 until 1967. During the years 1946 through 1952, I was Senior Accountant or Supervisor in charge of the First Securities audits, and have personal knowledge of all auditing procedures followed by Ernst & Ernst in such audits. During such years, I was fully familiar with the books and records, accounting methods and procedures, and the systems of internal control maintained by First Securities, and, in connection with such audits, I dealt with Leston B. Nay and Roy E. Campbell, President and Cashier respectively of First Securities.

4. All customers of First Securities whose accounts reflected long or short securities positions, cash positions other than zero, or open contractual commitments as of the annual audit date were sent a request from First Securities initiated by Ernst & Ernst, for a written confirmation to be made directly to Ernst & Ernst as to the accuracy of the statement of their accounts with First Securities. All such confirmation requests and the responses to them for audits during the years 1946 through 1952 have subsequently been disposed of in the usual course of business by Ernst & Ernst. No customers at any

time ever informed Ernst & Ernst that their securities positions, account balances, or statements of open contractual commitments, were incorrect because they did not reflect transactions or positions with respect to the alleged "escrow" or that any amount of "escrow" investments were owed to them by First Securities.

5. At no time did Ernst & Ernst prepare or examine the personal financial statements or tax returns of Leston B. Nay ("Nay") nor did Ernst & Ernst otherwise perform personal services for Nay individually. I did not have, and to my knowledge, no other partner, employee or agent of Ernst & Ernst ever had, knowledge of Nay's financial position or his obligations to any of the plaintiffs, or of any transactions or dealings between Nay and any of the plaintiffs prior to Nay's death in June 1968.

6. At no time prior to Nay's death did I, nor, to my knowledge, did any other partner, employee or agent of Ernst & Ernst, have any knowledge of any escrow, fictitious or nonexistent or otherwise, as described in the proceedings herein, or of any other escrow in which the plaintiffs invested or thought they were investing nor did I, nor to my knowledge, did any other partner, employee or agent or Ernst & Ernst, have any knowledge, prior to Nay's death, that Nay had obtained funds from the plaintiffs, had issued to the plaintiffs receipts, letters, or other written instruments relating to the "escrow" or investments therein, or had paid interest, reimbursed principal, disbursed funds, or otherwise had any transactions with the plaintiffs relating in any way to the alleged "escrow."

7. I was not, nor, to my knowledge, was any other partner, employee, or agent of Ernst & Ernst, ever contacted by any plaintiff requesting information regarding the "escrow."

8. Prior to Nay's death, I did not, nor, to my knowledge, did any other partner, employee, or agent of Ernst & Ernst, have any knowledge of any of the correspondence between plaintiffs and Nay regarding the "escrow," or the fraud alleged by plaintiffs, or any of the acts or omissions of Nay constituting a part of or relating to the alleged fraud upon the plaintiffs.

Further affiant sayeth not.

/s/ L. E. Kist
LeRoy E. Kist

Subscribed and sworn to
before me this 8th
day of December, 1972.
/s/ Barbara J. Gorski
Notary Public

IN THE UNITED STATES DISTRICT COURT

• • (Caption—Nos. 71 C 454 and 71 C 1204) • •

EXHIBIT E

AFFIDAVIT OF JAMES M. AHERN

JAMES M. AHERN, duly sworn, on oath states as follows:

1. I have knowledge of the facts set forth below and will testify to such matters if called as a witness in the matter of Hochfelder vs. Midwest Stock Exchange and Ernst & Ernst, No. 71 C 454, and Martin v. Midwest Stock Exchange and Ernst & Ernst, No. 71 C 1204, both matters being heard in the United States District Court, Northern District of Illinois, Eastern Division.

2. I am presently employed as Assistant Director of District No. 8 of the National Association of Securities Dealers, Inc. (the "NASD"), which offices are located in Chicago, Illinois, and which district presently comprises the states of Illinois, Indiana, Iowa, Michigan, Minnesota, North Dakota, South Dakota and Wisconsin.

I have been continuously employed by the NASD since June, 1956 in the position of examiner, supervisor and assistant director.

3. The NASD is a non-profit membership corporation organized under the laws of the State of Delaware and is a self regulatory association registered with the Securities and Exchange Commission pursuant to Section 15A of the Securities Exchange Act of 1934. Its main function is that of self regulation of its membership consisting solely of brokers and dealers by the enforcement of its own rules and regulations set forth in its Rules of Fair Practice and certain of the rules and regulations of the Securities and Exchange Commission and the Federal Reserve Board. In fulfilling this function, the NASD maintains a regular examination program involving the periodic inspection of all member firms and a general examination of each member's books, records and business procedures. Such examinations are conducted by the staff of the District Office of the District in which such member is located. Attached hereto as Exhibit A is a copy of the examination report and interview form used by NASD examiners in connection with regular examinations of the books and records of its members during 1967, consisting of five pages.

4. As Assistant Director of the District No. 8 Office, I have access to and custody of the records and the files of the NASD with respect to its examinations of members located in this District. First Securities Company of Chicago ("First Securities") became a member of the NASD effective August 22, 1939 and remained a member until December 26, 1969. It was subject to examination by examiners of District No. 8 for, among other things, compliance with the Rules of Fair Practice, in-

cluding Section 27 thereof, and as reflected in NASD records and files located in the District No. 8's Chicago Office, the following examinations of First Securities were conducted:

1. 1944 - 1946
2. 1949 - Staff Exam
3. 1954 - Staff Exam
4. 1956 - Staff Exam
5. 1959 - Staff Exam
6. 1962 - Staff Exam
7. 1964 - Staff Exam
8. 1967 - Staff Exam

No serious apparent violations of any of the Sections of the Rules of Fair Practice were noted on the reports of examination.

Further affiant sayeth not.

/s/ James M. Ahern
James M. Ahern

Subscribed and Sworn to before me
this 6th day of December, 1972.
/s/ Andrew F. Atanowsky
Notary Public
Expires June 2, 1973

EXHIBIT A

EXAMINATION REPORT - PAGE 1

INTERVIEW

THIS OFFICE IS A: MAIN OFFICE _____ OSJ _____ NON-OSJ BRANCH OFFICE _____

1. DATE(S) CONDUCTED _____ 2. DISTRICT NO. _____

3. MEMBER _____

4. FULL ADDRESS _____

5. INTERVIEWED _____ 6. TITLE _____

7. PROP. _____ PART. _____ CORP. _____ 8. # OF BR. OFF. _____ REGISTERED _____

9. OSJs _____ LIST OFFICES SUPERVISED BY EXAMINED OFFICE _____

10. TOTAL PERSONNEL _____ # OF PRINCIPALS _____ # OF R.R.'S _____

11. EXCHANGE MEMBERSHIPS NYSE _____ ASE _____ BSE _____ MSE _____ PBSE _____ PCSE _____ OTHERS _____

12. TYPE OF BUSINESS (GIVE APPROX. % OF GROSS VOLUME ORS OF TRADES IF AVAILABLE)
OTC PRINCIPAL RETAIL _____ (INCLUDE LISTED SECURITIES TRADED OTC) WHOLESALE _____
OTC AGENT _____ (INCLUDE LISTED SECURITIES TRADED OTC) LISTED _____ (TRANS. EXECUTED ON AN EXCHANGE)

APPROX. PERIOD INV. CO. SHARES

MEMBER'S ESTIMATE BASED ON _____ CASH BASIS _____ CONTRACTUALS _____ VOLUNTARIES _____
UNDERWRITINGS & SELL GROUPS _____ EXEMPTS _____
AFFILIATED COMPANIES OR OTHER BUSINESSES _____

13. OTC PRINCIPAL - (INCLUDE LISTED SECURITIES TRADED OTC)
PROF. TRADING - APPROX. NUMBER OF ISSUES _____ PRICE RANGES OF ISSUES TRADED _____ NUMBER OF NOB LISTINGS _____

PRIN. TRANS. W/CUST. - SIMULTANEOUS BASIS _____ FROM POSITION (MARKET MAKERS) _____ NOM POSITIONS MAINTAINED PRIMARILY FOR RETAIL PURPOSES _____

14. LISTED BUSINESS (AGENCY ORDERS EXECUTED THROUGH EXCHANGE MEMBE

COMM. POLICY - NYSE RATE _____ WITH OVER-RIDES OF _____ OTHER _____

(FOR NON-EXCHANGE FIRMS) NAMES OF EXCHANGE MEMBERS EXECUTING _____

Note - Form EX-100A by item number all apparent violations or irregularities.

FORM EX-100-1 (7-65)

BEST COPY AVAILABLE

EXHIBIT A — EXAMINATION REPORT – PAGE 2 — INTERVIEW (Cont'd)

1. DATE(S) CONDUCTED _____ MEMBER _____

19. OTC AGENCY (INCLUDE LISTED SECURITIES TRADED OTC)

COMM. RATE: NYSE _____ OTHER _____

METHOD OF OBTAINING BEST AVAILABLE MARKET _____

16. INV. CO. SHS. BUY FROM SPONSORS ONLY _____ OTHER SOURCES _____ TAKE POSITION _____

REDEMPTION POLICY: NO CHARGE _____ COMM. _____ OTHER CHARGE _____

REDEEMED THROUGH: FIRM _____ UNDERWRITER DIRECT _____

17. CLIENTELE RETAIL INDIVIDUAL _____ INSTITUTIONAL _____ B/D _____

18. TYPES OF A/C'S CASH _____ MARGIN _____ DISCRETIONARY _____

INV. ADVISORY _____ OTHER _____

19. FINANCING OF BUSINESS CASH BASIS _____ OMNIBUS A/C FOR WITH OTHERS _____ COLLATERAL LOANS WITH _____

20. CLEARANCE OTC SELF _____ THRU/FOR OTHERS _____

LISTED SELF _____ THRU/FOR OTHERS _____

21. LIST NAMES OF WIRE CONNECTIONS _____

22. SUPERVISION IN WRITING BY WHOM _____ (TRANSACTIONS) _____ (CORRESPONDENCE) TRANSACTIONS EVIDENCED ON _____ (NAME OF RECORD)

HOW OFTEN DOES FIRM REVIEW NON-DISCRETIONARY A/C'S _____ DISC. A/C'S _____

WHEN ARE DISCRETIONARY ORDERS APPROVED _____

HOW OFTEN ARE OS/S INSPECTED _____

23. ADVERTISING GEN. ADV. - MEDIA USED _____ FAMILIAR WITH FILING REQ. _____

INV. CO. - ADV. MEDIA USED _____ FAMILIAR WITH FILING REQ. _____

Note on Form EX-100A by item number all apparent violations or irregularities.

FORM EX-100-2 (7-65)

EXHIBIT A — EXAMINATION REPORT – PAGE 3 — EXAMINATION

1. DATE(S) CONDUCTED _____ MEMBER _____

24. RECORDS MADE AVAILABLE BY _____ (NAME) _____ (TITLE)

CONFIRMATIONS 25. CAPACITY DISC. _____ 26. DUAL AGENCY _____ 27. UPC SEC. 9 _____

28. HYPOTHECATION LEGEND _____ 29. AGENCY LEGEND _____ 30. COPIES KEPT _____

PRINCIPAL TRANSACTIONS 31. SIMULTANEOUS BASIS _____ SCHEDULE "A" NO. OF TRANS. _____

SCHEDULE "B" NO. OF TRANS. _____

32. FROM POSITION _____ SCHEDULE "A" NO. OF TRANS. _____

SCHEDULE "B" NO. OF TRANS. _____

IRREGULAR ACTIVITIES 33. SECRET PROFIT _____ 34. GUARANTEEING CUSTS. AGAINST LOSS _____ 35. OTHER _____

AGENCY TRANSACTIONS 36. COMMISSION RATES _____ 37. ANY EVIDENCE OF IRREGULARITIES _____

INVESTMENT CO. AREAS 38. PUBLIC OFFERING PRICE MAINTAINED _____ 39. LETTERS OF INTENT BREAKPOINTS, ETC. _____ 40. SEC. 26(F) (1) AND (2) _____ _____

41. SELLING DIV. _____ 42. SWITCHING _____ 43. _____

SALES MEMOS 44. FILE MAINTAINED _____ 45. TIMED ON ENTRY _____ 46. TIMED ON EXEC./CANC. _____ 47. CANCELLED ORDERS KEPT _____

LOCATION OF PRIMARY BOOKS AND RECORDS _____. IF THIS OFFICE MAINTAINS ANY OF THE FOLLOWING RECORDS AND THEY ARE DUPLICATES OF THE PRIMARY RECORDS, ANSWER "DUP." (DUPLICATE) IN THE BLANK SPACE. NOTE ANY APPARENT DISCREPANCIES ON EX 100A.

BLOTTERS 48. PURCH. & SALES _____ 49. SEC. REC. & DEL. _____ 50. CASH. REC. & DISB. _____

LEDGERS 51. GEN. LEDGER _____ 52. CUST. LEDGER _____ 53. POSITION RECORD _____

OTHER RECORDS 54. B/D FAIL RECORD (CHECK ONE) _____ OR REG. B/D LEDGER _____ 55. MO. TRIAL BALANCE _____ 56. CUST. A/C REC. _____

57. ASSOC. PERSON APPLICATION _____ 58. A/C'S CURRENT _____ 59. BASIS Y _____ S _____

60. MISCELLANEOUS _____

Note on Form EX-100A by item number all apparent violations or irregularities.

FORM EX-100-3 (7-65)

EXHIBIT A — EXAMINATION REPORT – PAGE 4 — EXAMINATION (Cont'd)

1. DATE(S) CONDUCTED _____ MEMBER _____

FILES

61. CUST. COMPLAINT _____ 62. INV. CO. ADV. & SALES LIT. _____ 63. GEN. ADV. & SALES LIT. _____ 64. CORRES. _____

65. FILES CHECKED _____ COPIES ATTACHED _____ USE OF ASS'N. NAME _____

SUPERVISION

66. TRANS. EVIDENCED ON _____ 67. CORRES. _____ 68. WRITTEN SUPERVISORY PROCEDURES ON FILE _____

69. ANY EVIDENCE OF PERIODIC REVIEW OF CUSTOMER A/C'S _____ 70. ANY EVIDENCE OF ANNUAL INSPECTION OF EACH OSJ _____ 71. ANY EVIDENCE OF CERTIFICATION PROCEDURES FOR R.R.'S _____

FINANCIAL CONDITION

72. CAPITAL _____ (GROSS OR ADJ. NET) SOURCE _____ DATED _____

73. MINIMUM CAPITAL CATEGORY _____ 74. COMPLIANCE 15C3-1 _____ 75. SUBORD. AGREE. FILED _____

ASSESSMENT REPORT

CHECK THE MOST CURRENT REPORT AND IF IRREGULARITIES ARE NOTED, CHECK THE TWO PRECEDING REPORTS FOR ACCURACY. AMENDED REPORTS SHOULD BE SENT DIRECTLY TO THE TREASURER'S DEPARTMENT

REGISTERED REPRESENTATIVES

76. HANDLING TRANSACTIONS PRIOR TO REGISTRATION _____ 77. REQUIRE REGISTRATION _____ 78. REQUIRE TERMINATION _____

IF THERE ARE ANY REQUIRED ADDITIONS OR TERMINATIONS OF REGISTERED REPRESENTATIVES, MAIL EX-151 DIRECTLY TO THE MEMBERSHIP DEPARTMENT

CHURNING

79. # OF A/C'S CHECKED _____ ALPHABET LETTERS _____ PERIOD COVERED _____ APPARENT IRREGULARITIES _____

REG. T.

80. # OF A/C'S CHECKED _____ ALPHABET LETTERS _____ PERIOD COVERED _____ APPARENT IRREGULARITIES _____

IF VIOLATIONS ARE NOTED, APPROXIMATE # OF PURCHASES BY CUSTOMERS REVIEWED _____

DISCRETIONARY ACCOUNTS

81. # OF DISC. ACCOUNTS _____ # OF ACCOUNTS CHECKED _____ APPARENT IRREGULARITIES _____

82. WRITTEN AUTH ON FILE _____ 83. ANY EVIDENCE OF PROMPT APPROVAL OF ORDERS _____

84. ANY EVIDENCE OF FREQUENT REVIEW OF ACCOUNTS _____ 85. AGE & OCCUP. OF CUSTOMER RECORDED _____

FREE-RIDING

86. ISSUES CHECKED _____ APPARENT IRREGULARITIES _____

Note on Form EX-100A by item number all apparent violations or irregularities.

FORM EX-100.4 (7-65)

EXHIBIT A — EXAMINATION REPORT – PAGE 5 — EXAMINATION (Cont'd)

1. DATE(S) CONDUCTED _____ MEMBER _____

CUSTOMERS' SECURITIES

87. LENDING CUSTOMERS' SECURITIES _____ REQUIRED AUTH. SEC. 15(b) & (c) _____ 88. HYPOTHECATION _____

88. SYSTEM FOR SEG. & IDENT. CUSTOMERS' SECURITIES _____ APPROX. # OF SEG. A/C'S _____ # OF A/C'S CHECKED _____

CUSTOMERS' FREE CREDIT BALANCES (15C3-3)

90. PROCEDURE TO NOTIFY CUSTOMER _____ SEGREGATED BANK ACCOUNT _____

GEN. ADV. & SALES LIT.

91. ADV. FILED FOR REVIEW _____ FILES CHECKED _____ COPIES ATTACHED _____

INV. CO. ADV. & SALES LIT.

92. FILED FOR REVIEW _____ FILES CHECKED _____ COPIES ATTACHED _____

SHARING IN CUSTOMER'S A/C'S

93. NO. OF A/C'S _____ AUTHORIZATIONS ON FILE _____ 94. NO. OF A/C'S REVIEWED _____ 95. APPARENT IRREGULARITIES _____

TRANSACTIONS WITH EMPLOYEES OF OTHER MEMBERS

96. # OF A/C'S CHECKED _____ EMPLOYER MEMBER(S) NOTIFIED _____

NON-MEMBER TRANSACTIONS

97. _____

INTRASTATE U/W

98. _____ DOCUMENTS FILED _____

TIME: MEMBER'S OFFICE _____

EXAM. REPORT _____ EXAMINER(S) _____

_____

Note on Form EX-100A by item number all apparent violations or irregularities.

FORM EX-100.5 (7-65)

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454 and 71 C 1204) * *

EXHIBIT F

AFFIDAVIT OF JOHN F. WALSH

JOHN F. WALSH, duly sworn, on oath states as follows:

1. I have personal knowledge of the facts set forth below and would testify competently to such facts if called as a witness in these proceedings.

2. I am a certified public accountant licensed by the State of Illinois and have engaged in the full time practice of accountancy with the firm of Haskins & Sells continuously since 1953. From 1953 until 1963, I held the position of Staff Accountant with Haskins & Sells. From 1963 until 1969, I held the position of Principal, and in 1969 I was admitted to parnership and have been a partner with the firm of Haskins & Sells since that year.

3. I was graduated from Loyola University in 1951, when I received from that school the degree of Bachelor of Science in Commerce. From 1951 to 1953, I was in the United States Army. Since 1953 when I joined Haskins & Sells, I have been primarily engaged in the audits of brokers and dealers in securities. I am presently the Haskins & Sells partner responsible for all securities broker or dealer audits conducted by its Chicago office and as such I am responsible for the supervision of, and am fully familiar with, the conduct of all such audits of securities brokers or dealers undertaken by the Chicago office of Haskins & Sells. I am a past Chairman of the Section on Securities Broker-Dealers of the Specialized Industries Committee of the Illinois Society of Certified Public Accountants. I have also been a member of the Certified Public Accountants Advisory Committee to the Securities Division of the Office of the Secretary of State of Illinois.

4. The accounting firm of Haskins & Sells maintains 82 offices and sub-offices in the United States and engages in the general practice of auditing and accounting. One of the specializations of our firm is the audit of securities brokers or dealers. In that regard, our firm performs audit services for approximately 200 securities brokers or dealers, approximately 70 of which are members of either the New York Stock Exchange or the American Stock Exchange. To my knowledge, our firm maintains the largest auditing and accounting practice for securities brokers or dealers of any accounting firm in the United States. In connection with my positions as staff accountant, principal and partner responsible for audits of securities brokers or dealers conducted by the Chicago office of Haskins & Sells, I have participated in and continue to participate in the creation, dissemination and implementation of our firm's policies and procedures for audits of securities brokers or dealers throughout the United States. As a result, I am not only directly familiar with the audits of securities brokers or dealers conducted by the Chicago office of Haskins & Sells but have substantial knowledge of the accounting and auditing procedures and practices generally with respect to all audits of securities brokers or dealers by Haskins & Sells throughout the United States.

5. I presently supervise the conduct of the audits of 19 securities brokers or dealers, 6 of which are members of the New York Stock Exchange and 8 of which are members of the Midwest Stock Exchange. In addition, I supervise a portion of the audits of 13 other securities brokers or dealers which are members of national securities exchanges but whose principal place of business is located outside of the Chicago area. To my knowledge, the Chicago office of Haskins & Sells conducts the audits

of substantially more securities brokers or dealers than does the Chicago office of any other accounting firm.

6. The auditing and accounting standards and requirements, including those relating to systems of internal control, which were in existence from prior to 1957 through 1967 with respect to brokers or dealers in the public securities business who were members of the Midwest Stock Exchange, were largely derived from and expressed in the following: (a) Section 17 of the Securities Exchange Act of 1934, Rule 17a-5 and Form X-17a-5 promulgated thereunder by the Securities and Exchange Commission ("SEC"), (b) Midwest Stock Exchange Financial Questionnaire and Instructions of the Midwest Stock Exchange ("Exchange") referred to in said Questionnaire, (c) "Audits of Brokers or Dealers in Securities" issued by the Committee on Auditing Procedure of the American Institute of Certified Public Accountants (1956), (d) "Auditing Standards and Procedures, Statements on Auditing Procedure No. 33" issued by the Committee on Auditing Procedure of the American Institute of Certified Public Accountants (1963), and (e) various other treatises and authorities on accounting and auditing procedures and standards. I am fully familiar with the foregoing rules and authorities.

7. Ernst & Ernst has submitted to me records and documents which it has represented to me are all of the records and documents retained by it with respect to its audits of First Securities Company of Chicago ("First Securities") in its possession prior to the commencement of these proceedings. I reviewed and am familiar with all such records and documents relating to the 1967 audit of First Securities and reviewed the audit programs and calendars provided for the audits of First Securities for the years 1960 through 1966. I have also reviewed

the affidavits of Jerry M. Hooker, Newell P. Crockett, LeRoy E. Kist, and Roy E. Campbell filed in these proceedings. I am aware of the office rule of First Securities relating to mail addressed to Leston B. Nay ("Nay") personally or to the attention of Nay as that rule is described in the affidavit of Roy E. Campbell and am also aware of the borrowings of Nay from the company as reflected on the financial statements of First Securities reported on by Ernst & Ernst from 1960 through 1967. On the basis of the aforementioned materials and my examination thereof and my personal familiarity of auditing standards and procedures with respect to audits of securities brokers or dealers, I am able to form an opinion concerning the adequacy, under generally accepted auditing standards, of Ernst & Ernst's audits of First Securities. In my opinion the audit of First Securities conducted by Ernst & Ernst as of the fiscal year 1967 and its report on the financial position of First Securities as of October 31, 1967 was made in accordance with generally accepted auditing standards, as prescribed by Rule 17a-5 and Form X-17a-5 of the SEC and the other authorities referred to in paragraph 6 hereof, and included a review of the accounting system of First Securities, its internal accounting control and procedures for safeguarding securities in accordance with such standards and authorities. It is also my opinion that the audit programs and calendars provided for the audits of First Securities for the years 1960 through 1966, which programs and calendars were substantially similar to those provided and followed by Ernst & Ernst in 1967 (except to the change in 1964 to the surprise date of audit), met generally accepted auditing standards, and on the assumption that Ernst & Ernst implemented such procedures during such years (an assumption which I

believe, from my review and examination, to be reasonable), then in my opinion the audits of First Securities by Ernst & Ernst during such years also met generally accepted auditing standards notwithstanding any lack of inquiry into the First Securities office rules regarding the handling of mail addressed to Nay personally or to his attention.

8. Based on my review of the affidavits filed herein and the materials submitted to me by Ernst & Ernst, I am also able to form an opinion concerning the adequacy of the internal accounting controls of First Securities for the years 1960 through 1967. My opinion specifically assumes the existence of an office rule, maintained by the President of First Securities, requiring that all mail addressed to him personally or to his attention be opened only by him and prohibiting any person other than the President from opening mail addressed to him personally or to his attention. In my opinion, for the years 1960 through 1967, the system of internal accounting control maintained at First Securities contained sufficient procedures and measures to safeguard the firm's assets and to check the accuracy and reliability of its accounting data so that, in no circumstances, would the existence of a procedure with respect to mail, as described above and in Mr. Campbell's affidavit, be relevant or determinative of the existence or lack of internal accounting control for any purpose, including for purposes of comments by auditors to regulatory bodies or national securities exchanges, in connection with an accountant's expression of his opinion on the financial statements of a broker or dealer in securities. I am familiar with the internal accounting controls and procedures of a substantial number of the securities brokers or dealers audited by the Chicago office of Haskins & Sells during the years 1953 to 1963

and am familiar with the internal accounting controls and procedures of substantially all of the securities brokers or dealers audited by the Chicago office of Haskins & Sells during the years 1963 through 1967. To my knowledge, no such client of Haskins & Sells with whose procedures I am familiar prohibited its officers from opening mail addressed to them personally or to their attention or required a third party control of such mail.

9. An examination by independent auditors to determine compliance with the rules and regulations of the National Association of Securities Dealers, Inc. ("NASD"), including its Rules of Fair Practice, is not and has never been within the scope of a regular annual audit of the financial condition of an NASD member by a certified public accountant. Neither the NASD, the SEC, nor any national securities exchange or any other authority requires the independent certified public accountants engaged in a regular annual audit of an NASD member to examine or report on compliance with the rules and regulations of the NASD, including its Rules of Fair Practice.

Further affiant sayeth not.

/s/ John F. Walsh
John F. Walsh

Subscribed and sworn to
before me this 18th day
of December, 1972.
/s/ Estello Singer
Notary Public

For Release in MORNING Newspapers of Saturday November 28, 1942

SECURITIES AND EXCHANGE COMMISSION
Philadelphia

SECURITIES EXCHANGE ACT OF 1934
Release No. 3330

Brokers or dealers registered under the Securities Exchange Act of 1934 and members of national securities exchanges who do business with the public will be required to file annually with the Securities and Exchange Commission a statement of their financial condition under a new rule announced by the Commission today and effective immediately.

The form adopted by the Commission for use in filing such statements is the standard type of financial questionnaire which it is expected will be used by other regulatory bodies requiring financial reports from brokers or dealers and members of exchanges.

This questionnaire is an outgrowth of several months discussion held in various parts of the country between the Commission's staff and the Committee on Uniformity of the National Association of Securities Commissioners, the National Association of Securities Dealers, Inc., the Investment Bankers Association of America, the Association of Stock Exchange Firms, the national securities exchanges, the American Institute of Accountants, the Commodity Exchange Administration, and certain independent accountants expert in brokerage and investment house accounting.

It has been estimated by representatives of the securities industry that the adoption by all regulatory bodies of a standard form of questionnaire would result in a savings of approximately $500,000 annually to brokers and dealers.

The Commission's new rule is known as Rule X-17A-5. In general it requires brokers and dealers to submit reports of financial condition to the Commission at least once each year on the new Form X-17A-5. It specifies certain cases under which the reports must be certified by an independent public accountant, and contains requirements with respect to the qualifications of accountants and the information to be contained in the accountant's certificate.

While the Commission's rule becomes effective immediately, no reports need be filed before January 1, 1943.

The text of the Commission's action follows:

The Securities and Exchange Commission, deeming it necessary for the exercise of the functions vested in it and necessary and appropriate in the public interest and for the protection of investors so to do, pursuant to authority conferred upon it by the Securities Exchange Act of 1934, particularly Sections 17 and 23 (a) thereof, hereby takes the following action:

I. Adopts Rule X-17A-5, reading as follows:

RULE X-17A-5. REPORTS TO BE MADE BY CERTAIN EXCHANGE MEMBERS, BROKERS AND DEALERS.

(a) *Reports To Be Made Annually.* Every member of a national securities exchange who transacts a business in securities directly with others than members of a national securities exchange, and every broker or dealer who transacts a business in securities through the medium of any such member, and every broker or dealer registered pursuant to Section 15 of the Securities Exchange Act of 1934, as amended, shall file an Form X-17A-5, during each calendar year commencing January 1, 1943, a report of his financial condition as of a date not more than 45 days prior to the filing thereof, provided that reports for any two consecutive years shall not be filed within less than four months of each other. The report shall be filed in duplicate with the Regional Office of the Commission for the region in which the member, broker, or dealer has his principal place of business.

(b) *Nature and Form of Reports.* Each report of financial condition filed pursuant to paragraph (a) hereof shall be prepared and filed in accordance with the following requirements:

(1) The report of a member, broker, or dealer shall be certified by a certified public accountant or a public accountant who shall be in fact independent (A) if said member, broker, or dealer is required to file a certified financial statement with any agency of any state in which he does business as a condition of doing business in securities therein, or is required to file a certified financial statement with any national securities exchange of which he is a member, or (B) if, during the year preceding the date as of which his financial condition is reported said member, broker, or dealer has made a practice of (i) extending credit in any form to customers (such as carrying margin accounts or selling securities on a partial payment or installment basis): *Provided*, that credit shall not be deemed to be extended by reason of a bona fide delayed delivery of any such security against full payment of the entire purchase price thereof upon such delivery within thirty-five (35) days after such purchase; (ii) holding securities owned by customers, except as an incident to transactions with or for customers which are promptly consummated by delivery, or (iii) carrying credit balances of customers, except as an incident to transactions with or for customers which are promptly consummated by payment;

(2) Attached to the report shall be an oath or affirmation that, to the best knowledge and belief of the person making such oath or affirmation, (A) the financial statement and supporting schedules are true and correct and (B) neither the member, broker, or dealer, nor any partner, officer, or director, as the case may be, has any proprietary interest in any account classified solely as that of a customer. The oath or affirmation shall be made before a person duly authorized to administer such oaths or affirmations. If the member, broker, or dealer is a sole proprietorship, the oath or affirmation shall be made by the proprietor; if a partnership, by a general partner; or if a corporation, by a duly authorized officer.

(c) *Use of Statements Filed with State Commissions and National Securities Exchanges.* Any member, broker, or dealer who is subject to the provisions of paragraph (a) hereof may file in lieu of the report required by that paragraph a copy of any financial statement which he is, or has been, required to file with any national securities exchange of which he is a member, or

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with any agency of any State as a condition of doing business in securities therein, provided that (1) the copy so included reflects his financial condition as of a date not more than forty-five (45) days prior to the filing thereof with the Commission; and (2) the report, as filed with this Commission, meets the requirements of this rule and Form X-17A-5 and contains the information called for by that form.

(d) *Extension of Time for Filing Reports.* In the event any member, broker, or dealer finds that he cannot file his report for any year within the time specified in paragraphs (a) or (c) hereof without undue hardship, he may file with the Commission an application for an extension of time to a specified date which shall not be more than 30 days after the date as of which his financial condition is reported. The application shall state the reasons for the requested extension and shall contain an agreement to file the report on or before the specified date. The application shall be deemed granted unless the Commission, within ten days after receipt thereof, enters an order denying the application.

(e) *Exemptions.* Any "bank", as defined in Section 3 (a) (6) of the Act, shall be exempt from the provisions of this rule.

(f) *Qualifications of Accountants.* The Commission will not recognize any person as a certified public accountant who is not duly registered and in good standing as such under the laws of his place of residence or principal office. The Commission will not recognize any person as a public accountant who is not in good standing and entitled to practice as such under the laws of the place of his residence or principal office.

(g) *Accountant's Certificate.*

(1) Technical Requirements. The accountant's certificate shall be dated, shall be signed manually, and shall identify without detailed enumeration the items of the report covered by the certificate.

(2) Representations as to Audit. The accountant's certificate (A) shall contain a reasonably comprehensive statement as to the scope of the audit made, including a statement as to whether the accountant reviewed the procedures followed for safeguarding the securities of customers, and whether, if with respect to significant items in the report covered by the certificate any auditing procedures generally recognized as normal have been omitted, a specific designation of such procedures and of the reasons for their omission; (B) shall state whether the audit was made in accordance with generally accepted auditing standards applicable in the circumstances; and (C) shall state whether the audit made omitted any procedure deemed necessary by the accountant under the circumstances of the particular case.

(3) Nothing in this rule shall be construed to imply authority for the omission of any procedure which independent accountants would ordinarily employ in the course of an audit made for the purpose of expressing the opinions required by paragraph (h) of this rule.

(h) *Accountant's Certificate - Opinions to be Expressed.* The accountant's certificate shall state clearly the opinion of the accountant with respect to the financial statement covered by the certificate and the accounting principles and practices reflected therein.

(i) *Accountant's Certificate - Exceptions.* Any matters to which the accountant takes exception shall be clearly identified; the exception thereto shall be specifically and clearly stated; and, to the extent practicable, the effect of each such exception on the related item of the report shall be given.

11. Adopts Form X-17A-5 to be used to comply with Rule X-17A-5. Effective November 28, 1942.

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As Revised November 30, 1967

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM X-17A-5

Information Required of Certain Members, Brokers and Dealers Pursuant to Section 17 of the Securities Exchange Act of 1934 and Rule 17a-5 Thereunder

GENERAL INSTRUCTIONS

A. Rules as to use of Form X-17A-5:

1. This form shall be used by every member, broker or dealer required to file reports under Rule 17a-5(*a*). It is not to be used as a blank form to be filled in but only as a guide in the preparation of the report. No caption need be shown as to which the items and conditions are not present.

2. The name of the respondent and date of report shall be repeated on each sheet of the answers and schedules submitted.

3. If no answer is made to a question or subdivision thereof it shall constitute a representation that respondent has nothing to report.

B. Presentation of information (including definitions):

1. The information presented shall be sufficient to permit the determination of the financial condition of the respondent.

2. The valuations of customers' securities in segregation or safekeeping need not be included in the answers.

3. Use separate pairs of columns for ledger debit and ledger credit balances; long security and spot (cash) commodity valuations and short security and spot (cash) commodity valuations; net losses in future commodity contracts and net gains in future commodity contracts. All columns must be totaled. The total of debit balances must equal the total of credit balances. The total of long security and spot (cash) commodity valuations must equal the total of short security and spot (cash) commodity valuations; the total losses and the total gains in future commodity contracts must be in agreement after consideration of "commodity difference accounts." The answers to Questions 14, 15, and 16 shall not be included in the totals.

4. Security and spot (cash) commodity valuations and losses and gains in future commodity contracts shall be based upon current market prices; fractions and accrued interest may be omitted except where such procedure in the case of short positions would have a material effect upon net capital.

5. "Securities not readily marketable" shall be so designated. The term "securities not readily marketable" shall include, but not be limited to, (a) securities, except "exempted securities," for which there is no market on a securities exchange or no independent publicly quoted market; (b) securities which cannot be publicly offered or sold unless registration has been effected under the Securities Act of 1933 (or the conditions of an exemption such as Regulation A under Section 3(b) of such Act have been complied with); and (c) securities which cannot be offered or sold because of other arrangements, restrictions, or conditions applicable to the securities or to the respondent.

6. All accounts (other than regulated commodity accounts) of any one customer may be combined and reported under any appropriate classification other than Question 6.A. Customers' accounts related by bona fide written guarantees may be combined.

7. For the purpose of this questionnaire the term "customer" shall not include the respondent, general partners, officers, or directors. An account covered by a "satisfactory subordination agreement" shall be reported in answer to Question 12.

8. Foreign currency may be expressed in terms of U.S. dollars at the current rate of exchange and where carried in conjunction with the U.S. dollar balances

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for the same customer may be consolidated with such U.S. dollar balances and the gross or net position reported in its proper classification, provided the foreign currency is not subject to any restrictions as to conversion. If the foreign currency position so treated is substantial, some indication of its size shall be given.

9. If the respondent is a sole proprietor, all accounts carried by brokers, dealers, or others for the respondent which contain money balances and/or securities allocated to or otherwise used in connection with his business shall be reported in the answers to Questions 1 through 16, as appropriate.

10. "Exempted securities" are those securities defined as such under the provisions of Section 3(a)(12) of the Securities Exchange Act of 1934 other than securities designated for exemption by action of the Securities and Exchange Commission.

11. The term "contractual commitments" shall include underwriting, when-issued, when-distributed and delayed delivery contracts, repurchase agreements, endorsements of all puts and all calls, commitments in foreign currencies, and spot (cash) commodity contracts but shall not include future commodity contracts and uncleared "regular way" purchases and sales of securities. A series of contracts of purchase or sale of the same security conditioned, if at all, only upon issuance may be treated as an individual commitment.

12. For the purpose of this questionnaire securities sold as principal under an agreement to repurchase shall be stated separately and clearly indicated as such in the answers to Questions 3.A. and 10.

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...ase X-17A-5 U.S. SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 3

FACING PAGE

Form X-17A-5 — Information Required of Certain Members, Brokers and Dealers Pursuant to Section 17 of the Securities Exchange Act of 1934 and Rule 17a-5 Thereunder — SEC FILE NUMBER

FOR SEC USE

...ING LOCATION	DATE OF REPORT	DOCUMENT SEQ. NO.	

...ME OF REGISTRANT (If individual, state last, first, middle name) — I.R.S. Employer Identification or Social Security No.

...ME UNDER WHICH BUSINESS IS CONDUCTED (If different)

...DRESS OF PRINCIPAL PLACE OF BUSINESS (Number and Street; City; State; ZIP Code)

...ATTACHED REPORT reflects the financial condition of the above registrant as of (Date)

...PENDENT PUBLIC ACCOUNTANT whose Opinion is contained in this Report (Name (If individual, state last, first, middle name)) — I.R.S. Employer Identification or Social Security No.

Address (Number and Street; City; State; ZIP Code)

Check one—

- ☐ Certified Public Accountant
- ☐ Public Accountant
- ☐ Accountant not resident in United States or any of its possessions

FOR SEC USE

...REPORT CONSISTS OF (Check below)

- ☐ Part I—Financial Information
- ☐ Part II—Supporting Schedules
- ☐ Accountant's Certificate

DO NOT WRITE BELOW THIS LINE . . . FOR SEC USE ONLY

Part I

FINANCIAL QUESTIONNAIRE

Question 1—Bank Balances and Other Deposits.

State separately total of each kind of deposit (cash and/or market value of securities) with adequate description. This shall include cash on hand; cash in banks representing general funds subject to immediate withdrawal; cash in banks subject to withdrawal restrictions; funds segregated pursuant to regulations of any agency of the Federal Government, any State, any national securities exchange or national securities association; contributions to clearing organizations incident to membership; deposits with clearing organizations in connection with commitments; guaranty and margin deposits; good faith deposits (see note 3 to Question 14); drafts with securities attached deposited for collection.

Question 2—Money Borrowed, and Accounts Carried for Respondent by Other Banking or Brokerage Houses, Secured by or Containing Customers' Collateral.

State separately totals of ledger net debit balances; ledger net credit balances; long security valuations; short security valuations; spot (cash) commodity valuations; net losses and net gains in future commodity contracts, and classify as follows:

A. Money borrowed:

1. From banks, trust companies, and other financial institutions
2. From others.

B. Accounts carried for respondent by other banking or brokerage houses, including omnibus accounts:

1. Securities accounts:
   a. Accounts with net debit balances
   b. Accounts with net credit balances.
2. Commodities accounts.
   a. Regulated commodities futures accounts:
      i. Accounts liquidating to an equity
      ii. Accounts liquidating to a deficit.
   b. Nonregulated commodities futures accounts:
      i. Accounts liquidating to an equity
      ii. Accounts liquidating to a deficit.
   c. Spot (cash) commodity accounts:
      i. Accounts with net debit balances
      ii. Accounts with net credit balances.

Notes:

1. To the extent that the collateral for the loan, or other amount payable, also includes additional collateral owned by others than customers, the valuation of such collateral shall be shown separately and designated as owned by respondent, general partners, officers, directors, or others, including securities covered by subordination agreements.

2. If collateralized entirely by "exempted securities," the amount of the borrowing, or amount payable to a banking or brokerage house, and the valuation of the collateral shall be stated separately.

Question 3—Money Borrowed, and Accounts Carried for Respondent by Other Banking or Brokerage Houses, Unsecured, or Secured Entirely by Collateral Owned by Respondent and Its Partners or Its Officers and Directors, or by Securities Covered by "Satisfactory Subordination Agreements."

State separately totals of ledger net debit balances; ledger net credit balances; long security valuations; short security valuations; spot (cash) commodity valuations; net losses and net gains in future commodity contracts, and classify as follows:

A. Money borrowed:

1. From banks, trust companies, and other financial institutions
2. From officers and directors
3. From others.

B. Accounts carried for respondent by other banking or brokerage houses:

1. Securities accounts:
   a. Accounts with net debit balances
   b. Accounts with net credit balances.
2. Commodities accounts:
   a. Regulated commodities futures accounts:
      i. Accounts liquidating to an equity
      ii. Accounts liquidating to a deficit.
   b. Nonregulated commodities futures accounts:
      i. Accounts liquidating to an equity
      ii. Accounts liquidating to a deficit.
   c. Spot (cash) commodity accounts:
      i. Accounts with net debit balances
      ii. Accounts with net credit balances.

Note: State separately borrowings under A or credit balances under B.1.b. and/or B.2.c.n.:

1. Unsecured
2. Not adequately collateralized under Rule 15c3-1(c)(6)
3. Collateralized in whole or in part by securities and/or commodities reportable under 8 or 9.B. Designate valuation of such collateral and state separately amounts adequately collateralized by "exempted securities."

Question 4—Other Open Items With Brokers and Dealers.

State separately totals of ledger debit balances; ledger credit balances; long security valuations; short security valuations, and classify as follows:

A. Securities borrowed (i.e., amount to be received from others upon return to them of securities borrowed by respondent).

B. Securities failed to deliver (i.e., amount to be received from brokers and dealers upon delivery of securities sold by respondent).

C. Securities loaned (i.e., amount to be paid to others upon return of securities loaned by respondent):

1. Customers' securities
2. Securities reportable under 8 or 9.B.
3. Securities reportable under 9.A., 10, 11, and 12.

D. Securities failed to receive (i.e., amount to be paid to brokers and dealers upon receipt of securities purchased by respondent):

1. For customers
2. For accounts reportable under 8 or 9.B.
3. For accounts reportable under 9.A., 10, 11, and 12:
   a. Sold at date of report
   b. Unsold at date of report.

Notes:

1. Where it is impractical or unduly expensive to allocate all securities loaned and all securities failed to receive to each category in C and D, proper allocation shall be made to the extent feasible and all other such credit balances and short security valuations shall be reported under C.1. and/or D.1., respectively.

2. State separately or in a footnote, ledger debit balances, ledger credit balances, long security valuations, short security valuations, with respect to each security transaction outstanding 30 days or longer under Question 4.B., Securities Failed to Deliver, and Question 4.D., Securities Failed to Receive.

Question 5—Valuations of Securities and Spot (Cash) Commodities in Box, Transfer and Transit.

State separately the total valuation of:

A. Negotiable securities in box, transfer, and in transit between offices of respondent.

B. Spot (cash) commodities represented by warehouse receipts or bills of lading in box and in transit between offices of respondent.

Note: Question 5 requires entries in short valuation column only.

Question 6—Customers' Security Accounts.

State separately totals of ledger debit balances; ledger credit balances; long security valuations; short security valuations, and classify as follows:

A. Bona fide cash accounts (i.e., accounts having both unsettled money balances and positions in securities which are current items within the meaning of Section 4(c) of Regulation T of the Board of Governors of the Federal Reserve System):

1. Accounts with debit balances
2. Accounts with credit balances.

B. Secured accounts:

1. Accounts with debit balances
2. Accounts with credit balances.

C. Partly secured accounts (accounts liquidating to a deficit):

1. Accounts with debit balances
2. Accounts with credit balances.

D. Unsecured accounts.

E. Accounts with credit balances having open contractual commitments.

F. Accounts with free credit balances.

G. Fully paid securities not segregated.

Notes:

1. Cash accounts which are not "bona fide cash accounts" shall be reported under B, C, or D, as appropriate.

2. Do not combine the accounts of customers except as permitted by General Instruction B.6.

3. Each joint account carried by respondent in which respondent has an interest shall be so stated, separately, as a customer's account in the proper classification and the status of the respondent's interest therein shall be stated. Funds received by respondent as margin in these accounts shall be separately stated by account. If any funds have been provided by the respondent as margin, these shall be clearly indicated here and in the answer to Question 13.

4. With respect to contractual commitments state as a footnote or in a separate schedule the total of:

a. Deficits in the accounts of the respective customers reported in the answers to B and/or E after application of net losses in open contractual commitments in securities carried for each such customer.

b. Net losses in open contractual commitments in securities carried for each customer whose account is reported in the answers to C or D.

In computing net losses, gains at market and profits on such sales may be applied against losses only in the same security in each customer's account.

5. See General Instruction B.11 for definition of the term "contractual commitments."

Question 7—Customers' Commodity Accounts.

State separately totals of ledger debit balances; ledger credit balances; spot (cash) commodity valuations; net losses and net gains in future commodity contracts, and classify as follows:

A. Accounts with open future contracts liquidating to an equity:

1. Regulated commodities
2. Nonregulated commodities.

B. Accounts with open future contracts liquidating to a deficit:

1. Regulated commodities
2. Nonregulated commodities.

C. Accounts with spot (cash) commodity positions:

1. Hedged:
   a. Secured
   b. Partly secured.
2. Not hedged:
   a. Secured
   b. Partly secured.

D. Unsecured debit balance.

E. Accounts with free credit balances:

1. Regulated
2. Nonregulated.

Note: See notes 2 and 3 to Question 6.

Question 8—Accounts of Officers and Directors.

State separately, in accordance with the applicable classifications and instructions of Questions 6 and 7, totals of ledger debit balances; ledger credit balances; long security and spot (cash) commodity valuations; short security and spot (cash) commodity valuations; net losses and net gains in future commodity contracts in the accounts of:

A. Officers.

B. Directors.

Note: If an individual is both an officer and a director, classify the accounts under 8.A.

Question 9—General Partners' Individual Accounts.

State separately totals of ledger debit balances; ledger credit balances; long security and spot (cash) commodity valuations; short security and spot (cash) commodity valuations; net losses and net gains in future commodity contracts, and classify as follows:

A. Individual accounts of general partners who have signed specific agreements that cash, securities, commodities, and equities recorded in these accounts are to be included as partnership property.

B. All other accounts of general partners. (These accounts shall be classified in accordance with the applicable classifications and instructions of Questions 6 and 7.)

Notes:

1. Total valuations of "exempted securities" reported in answer to Question 9.A. shall be stated separately.

2. The noncapital accounts of partners other than general partners shall be included either with customers' accounts in the appropriate classifications of Questions 6 and 7 or, where applicable, in Question 12.

Question 10—Trading and Investment Accounts of Respondent.

State separately totals of ledger debit balances; ledger credit balances; long security and spot (cash) commodity valuations; short security and spot (cash) commodity valuations; net losses and net gains in future commodity contracts, and classify as follows:

A. Securities accounts:

1. Exempted securities
2. Other securities.

B. Commodities accounts:

1. Future commodities contracts
2. Spot (cash) commodities;
   a. Hedged
   b. Not hedged.

C. Other.

Notes:

1. Ledger balances may be combined with respect to all security accounts, and also with respect to all spot (cash) commodity accounts.

2. Treasury stock of respondent shall not be included hereunder.

3. In the case of a sole proprietor, see General Instruction B.9.

Question 11—Capital Accounts.

State separately totals of ledger debit balances; ledger credit balances; long security and spot (cash) commodity valuations, short security and spot (cash) commodity valuations, and classify as follows:

A. Sole proprietorship:

1. Capital account
2. Undistributed profit and loss accounts, including balances remaining in income and expense accounts. (This question may be answered by giving one net amount.)

B. Partnership:

1. Capital accounts of general partners
2. Capital accounts of special or limited partners
3. Undistributed profit and loss accounts, including balance remaining in income and expense accounts. (This question may be answered by giving one net amount.)

C. Corporation or similar entity:

1. Capital stock (detail by class of stock showing number of shares and par value):
   a. Authorized (state parenthetically)
   b. Issued
   c. Treasury stock.
2. Capital surplus
3. Earned surplus or deficit, including balances retaining in income and expense accounts. (This question may be answered by giving one net amount.)

D. Capital reserves. (State nature and amount of each reserve. Valuation reserves and liability reserves shall be reported in answer to Question 13.)

Note: Total valuations of "exempted securities" shall be stated separately.

Question 12—Subordinated Accounts.

State separately for all accounts covered by "satisfactory subordination agreements," totals of ledger debit balances; ledger credit balances; long security and spot (cash) commodity valuations; short security and spot (cash) commodity valuations; net losses and net gains in future commodity contracts, and classify as follows:

A. Subordinated accounts:
1. Accounts with debit balances
2. Accounts with credit balances.
3. Subordinated borrowings.

Notes:

1 Total valuations of "exempted securities" shall be stated separately.

2 Any subordinated account reported under this question must be subject to an agreement which complies with the requirements of Rule 15c3-1(c)(7) or, if the respondent is a member of an exchange whose members are exempt from Rule 15c3-1 by subparagraph (b)(2) thereof, complies with the rules regarding subordination agreements of all the exchanges therein listed of which respondent is a member. Subordinated accounts with agreements that do not comply with the above requirements must be reported in the answers to questions 2 through 9, as appropriate.

Question 13—Other Accounts, etc.

State details (ledger balances; valuations of securities and spot (cash) commodities; status of future commodity positions; and any other relevant information) of any accounts which have not been included in one of the answers to the above questions. These will include: accounts for exchange memberships; furniture, fixtures, and other fixed assets; valuation reserves; funds provided or deposited by the respondent as margin in joint accounts; revenue stamps; dividends receivable, payable, and unclaimed; floor brokerage receivable and payable; commissions receivable and payable; advances to salesmen and other employees; commodity difference account; goodwill; organization expense; prepaid expenses and deferred charges; liability reserves; mortgage payable; other liabilities and deferred credits; market value of securities borrowed (other than for delivery against customers' sales) to the extent to which no equivalent value is paid or credited; and other accounts not specifically mentioned herein.

Note: Any liability reported under this question secured by collateral in any form shall be identified by reference to the related collateral.

The responses to Questions 14, 15, and 16 shall not be included in the totals.

Question 14—Contractual Commitments That Are Not Recorded in a Ledger Account for Money.

State separately for each type of commitment total cost; total proceeds; valuation of the net long and/or short position for the following:

A. Respondent (see notes 2 and 3).

B. General partners who have signed specific agreements that cash, securities, commodities and equities recorded in these accounts are to be included as partnership property.

C. Subordinated accounts.

D. Other general partners, officers and/or directors:

1. Accounts not fully secured (including unsecured accounts)

2. Commitments which are substantial in view of the capital of the respondent.

E. Customers:

1. Accounts not fully secured (including unsecured accounts)

2. Commitments which are substantial in view of the capital of the respondent.

Notes:

1. See General Instruction B.11 for definition of term "contractual commitments."

2. As to underwriting commitments, the amounts reported shall represent the respondent's interest in the entire account.

3. Related good faith deposits shall be clearly indicated; the total thereof shall be included in the amount reported in answer to Question 1.

4. The details required by Part II(a) may be reported herein.

Question 15—Participations of the Respondent in Joint Trading and Investment Accounts Carried by Others That are not Recorded in a Ledger Account for Money.

State separately for each joint account (1) the account balance, exclusive of deposits; (2) the total market valuations of long securities, short securities, and commodities; and (3) the respondent's share of such account balance and each such market valuation. Any related deposits reported in answer to Question 13 shall be clearly indicated hereunder.

Question 16—Unrecorded Assets, Liabilities and Accountabilities.

Submit a separate schedule containing a description of any assets, liabilities and accountabilities of the respondent, actual or contingent, which are not included in a ledger account or reported in answer to Questions 14 and 15. Only such items which in the aggregate are material in relation to net capital need be reported. Accountabilities shall include cash and/or other property including securities held for customers by or on behalf of respondent, which are not included in a ledger account. Contingent liabilities may include lawsuits pending against the respondent, accommodation endorsements, rediscounted notes, and guarantees of accounts of others.

Part II

SUPPLEMENTARY INFORMATION

Submit the following information:

(a) Separate schedules giving adequate description including quantity, price, and valuation of each security and commodity position supporting each total valuation reported in answer to the following:

Questions 6 and 7—Joint accounts in which respondent has an interest.

Questions 6.C., 7.C.1.b., and 7.C.2.b.—Customers' partly secured accounts.

Question 8—Partly secured accounts of officers and directors.

Question 9A.—Individual accounts of general partners who have signed specific agreements that cash, securities, commodities, and equities recorded in these accounts are to be included as partnership property.

Question 9.B.—Partly secured accounts of partners reported in response hereto.

Question 10—Trading and investment accounts of respondent.

Question 11—Capital accounts.

Question 12—Subordinated accounts and borrowings.

The schedule shall show with respect to each borrowing or claim the name of the lender, the relationship to respondent, the amount of the borrowing or claim and the maturity date of the agreement.

Question 14—Contractual commitments that are not recorded in a ledger account for money reported in answer to Questions 14.A., 14.B., 14.C., 14.D.1., and 14.E.1., Part I.

In addition to the details of securities and commodities positions, report the total cost and total proceeds for each security and commodity; the totals thereof shall agree with the amounts reports in answer to Question 14, Part I.

Where contractual commitments exist in puts or calls, or any combination thereof, the details shall include separately with respect to puts or calls in each separate security of the same class: quantity, description of security, expiration date or range of expiration dates, indicated contract costs or proceeds, market valuation and indicated unrealized profit or loss. This information shall be reported in separate columns, classified separately and grouped as puts or calls.

Where contractual commitments are related to positions in other securities reflected in the answers to questions in Part I such relationship shall be clearly described.

The above information may be reported in Part II(a) or in the answer to Question 14, Part I.

Question 15—Participations of the respondent in joint trading and investment accounts carried by others that are not recorded in a ledger account for money.

Notes:

1. "Exempted securities" and "securities not readily marketable" shall be stated separately.

2. If the respondent is not exempt from the provisions of Rule 15c3-1 but desires that, where allowed, greater than 70 percent of the market valuation of certain securities be included in the computation of net capital under that rule, such securities shall either be listed by groups in accordance with the classifications of Rule 15c3-1(c)(2)(C) or the applicable percentages allowable under that rule shall be stated with respect to each security and a summary of valuations by such percentages shall be given.

(b) A schedule showing in detail ledger balances, valuations of long and short securities and spot (cash) commodities, and net losses and net gains in future commodity contracts and other open contractual commitments (other than those reported in the answers to Part I of this Form) in any accounts carried by other brokerage houses in which a sole proprietor or any general partner of the respondent has an interest

(Accounts containing only free securities or free credit balances need not be reported.)

(c) (i) A separate schedule showing the market value of all long and all short future commodity contracts in each account other than customers' commodity accounts reported in answer to all Questions in Part I of this Form (contracts representing spreads or straddles in the same commodity and those contracts offsetting or hedging any "spot" commodity positions, and accounts of general partners, officers or directors not subject to percentage deduction [Rule 15c3-1(c)(2)(D)] shall be so designated).

(ii) A separate schedule showing the market value of all customers' long and all customers' short future contracts in each commodity reported in answer to all Questions in Part I of this Form.

(d) If the answer to Question 11 includes amounts authorized or proposed to be distributed or withdrawn within the next 6 months, furnish the details.

(e) If respondent is a sole proprietor, state whether any liabilities which are not reflected in the answers to Part I of this Form would materially affect net worth as reported; if such liabilities would materially affect net worth as reported, the statement required by Item 7 of the Audit Requirements shall be furnished as a schedule.

(f) If the respondent has met the conditions specified in subparagraph (a)(2) of Rule 15c3-1 throughout the year and desires that the lower net capital requirements apply, a specific statement to that effect shall be furnished as a schedule.

AUDIT REQUIREMENTS

The audit shall be made in accordance with generally accepted auditing standards and shall include a review of the accounting system, the internal accounting control and procedures for safeguarding securities including appropriate tests thereof for the period since the prior examination date. It shall include all procedures necessary under the circumstances to substantiate the assets and liabilities and securities and commodities positions as of the date of the responses to the financial questionnaire and to permit the expression of an opinion by the independent public accountant as to the financial condition of the respondent at that date. Based upon such audit, the accountant shall comment upon any material inadequacies found to exist in the accounting system, the internal accounting control and procedures for safeguarding securities, and shall indicate any corrective action taken or proposed. These comments may be submitted in a supplementary certificate and filed pursuant to Rule 17a-5(b)(3).

The scope of the audit shall include the following procedures, but nothing herein shall be construed as limiting the audit or permitting the omission of any additional audit procedure which an independent public accountant would deem necessary under the circumstances. As of the audit date the independent public accountant shall:

(1) Compare ledger accounts with the trial balances obtained from the general and private ledgers and prove the aggregates of subsidiary ledgers with their respective controlling accounts.

(2) Account for by physical examination and comparison with the books and records: all securities, including those held in segregation and safekeeping; material amounts of currency and tax stamps; warehouse receipts; and other assets on hand, in vault, in box or otherwise in physical possession. Control shall be maintained over such assets during the course of the physical examination and comparison.

(3) Verify securities in transfer and in transit between offices of respondents.

(4) Balance positions in all securities and spot and future commodities as shown by the books and records at the audit date.

(5) Reconcile balances shown by bank statements with cash accounts. After giving ample time for clearance of outstanding checks and transfers of funds, the independent public accountant shall obtain from depositaries bank statements and canceled checks of the accounts and by appropriate audit procedures substantiate the reconciliation as of the audit date.

(6) Obtain written confirmations with respect to the following (see note):

(a) Bank balances and other deposits.

(b) Open contractual positions and deposits of funds with clearing corporations and associations.

(c) Money borrowed and detail of collateral.

(d) Accounts, securities, commodities, and commitments carried for the respondent by others.

(e) Details of:

(i) Securities borrowed

(ii) Securities loaned

(iii) Securities failed to deliver

(iv) Securities failed to receive

(v) Contractual commitments (see General Instruction B.11).

(f) Customers', partners', officers', directors', and respondent's accounts. Confirmation of these accounts may be in the form of a written acknowledgment of the accuracy of the statement of money balances, securities and/or commodities positions, and open contractual commitments (other than uncleared "regular way" purchases and sales of securities) accompanying the first request for confirmation mailed by the independent public accountant. Customers' accounts without balances, position or commitments, and accounts closed since the last prior audit shall be confirmed on a test basis.

(g) Borrowings and accounts covered by "satisfactory subordination agreements."

(h) Guarantees in cases where required to protect accounts guaranteed as of audit date.

(i) All other accounts which in the opinion of the independent public accountant should be confirmed.

Note: Compliance with requirements for obtaining written confirmation with respect to the above accounts shall be deemed to have been made if requests for confirmation have been mailed by the independent public accountant in an envelope bearing his own return address and second requests are similarly mailed to those not replying to the first requests, together with such auditing procedures as may be necessary; provided, however, that with respect to customers' accounts closed since the last prior audit the accountant may use either positive or negative confirmation requests; and it is further provided that with respect to periodic investment plans sponsored by member firms of a national securities exchange, whose members are exempted from Rule 15c3-1 by paragraph (b)(2) thereof, the independent public accountant examining the financial statements of the originating member firm may omit direct written confirmation of such plan accounts with customers when, in his judgment, such procedures are not necessary, if (1) the originating member firm does not receive or hold securities belonging to such plan accounts and does not receive or hold funds for such accounts, except the initial payment which is promptly transmitted to the custodian; (2) the custodian is a member firm of such national securities exchange and files certified reports complying with Rule 17a-5 in connection with which the customers' accounts are confirmed by an independent public accountant; and (3) funds and securities held by the custodian for each such customer's account are reconciled with the records of the originating member firm as of the date of the most recent audit of the custodian.

(7) Obtain a written statement from the proprietor, partner (if a partnership) or officer (if a corporation) as to the assets, liabilities, and accountabilities, contingent or otherwise, not recorded on the books of the respondent.

(8) Verify the computation of the ratio of aggregate indebtedness to net capital at the audit date and review the procedures followed in making the periodic computations required under the provisions of Rule 17a-3(a)(11).

NOTE: PROVISIONS OF RULE 17a-5 REQUIRE THAT THE REPORTS OF CERTAIN BROKERS AND DEALERS BE AUDITED BY A CERTIFIED PUBLIC ACCOUNTANT OR PUBLIC ACCOUNTANT WHO SHALL BE IN FACT INDEPENDENT. WITH RESPECT TO QUALIFICATIONS OF ACCOUNTANTS, ACCOUNTANT'S CERTIFICATE, OPINIONS TO BE EXPRESSED, AND EXCEPTIONS, PLEASE REFER TO RULE 17a-5.

U.S. GOVERNMENT PRINTING OFFICE: 1968 O—296-488

IN THE UNITED STATES DISTRICT COURT

• • (Caption No. 71 C 454 and No. 71 C 1204) • •

AFFIDAVIT OF MICHAEL K. GARST

1. I have knowledge of the facts set forth below and will testify to such matters if called as a witness in the above captioned cases.

2. I recently retired after twenty-five years of service as a National Bank Examiner. During my service, the questionnaire on Internal Controls was required to be answered by all National Bank Examiners, for each bank examined, and a copy sent to the FDIC and the Federal Reserve Bank as well as the Comptroller of Currency.

The question:

> "R 1. Are all Officers and employees required to be absent from the bank at least two consecutive weeks annually?"

was an important question because the essence of Internal Controls is duality of control. The duality purpose is indicated by many of the questions such as A1, A3, B3, C4, D2, D3 (a), F2, F3, F4, F7, K (b) and O. The rule requiring two weeks' absence is to assure such duality.

If I had encountered a case where the President of a bank had made a firm rule that, under no circumstances, could mail addressed to the bank for his attention be opened by anyone but him so that during his absence on vacation such mail piled up on his desk, I would have regarded that rule as a possible violation of duality of control and the purpose of the two weeks' absence re-

quirement and would have commented on it in the portion of the questionnaire labeled "Comments" at the end.

/s/ Michael K. Garst
Michael K. Garst

Subscribed and Sworn
to before me this
27th day of April, 1973.

/s/ Jerry H. Steurer
Notary Public

Charter No.....

INTERNAL CONTROLS

Where answer is negative, describe situation under Comments below and indicate possible corrective action. Reference to and elaboration on such comments, in necessary instances, should be made on Page 2.

ALL ANSWERS ARE YES UNLESS OTHERWISE NOTED

	Yes	No
A. CASH		
1. Is vault cash under dual control?		
(a) If not, are the safeguards by the bank reasonably adequate?		
2. Does each teller at all times have sole access to, and responsibility for the assigned cash?		
3. Is the cash of each teller verified at reasonably frequent intervals by another employee or officer?		
4. Is each teller required to maintain an ink or machine posted daily cash record?		
5. Are the following properly recorded, and scrutinized by an officer?		
(a) Cash items.		
(b) Over and shorts.		
B. DUE FROM BANKS		
1. Are cash letters received from all correspondent banks settled for promptly?		
2. Are statements received from correspondent banks at least monthly?		
3. (a) Are statements of the bank's accounts with other banks reconciled by the auditor or another employee (should not be the general ledger bookkeeper) who has no authority to draw against those accounts?		
(b) If not, are the verifications considered adequately protective?		
4. (a) Are correspondent bank account reconcilements verified by another officer or employee?		
(b) Are such verifications indicated on the bank's records?		
5. Is a permanent and adequate reconcilement record maintained?		
C. SECURITIES OWNED		
1. Is satisfactory register giving adequate detail maintained?		
2. Is the investment register periodically and independently proved to the general ledger?		
3. Are custody safeguards adequate?		
4. Are purchase and sale invoices independently verified by the auditor or another employee prior to being filed?		
D. LOANS AND DISCOUNTS		
1. Are loans and discounts proved to the general ledger at least monthly?		
2. Is proof made at least quarterly by other than employee having custody of notes?		
3. (a) Does an employee other than the note teller recheck interest and discount computations?		
(b) Are amounts verified with the general ledger?		
4. Are paid or renewed notes stamped or perforated paid or renewed?		
5. Are officers and employees prohibited from taking notes signed by a borrower in blank and held in anticipation of future borrowings?		
6. Does bank maintain a satisfactory collateral register?		
7. Are receipts obtained and filed (or does the collateral register show properly signed releases) for released collateral?		
8. Is custody of collateral properly safeguarded?		
9. (a) Does the bank maintain an adequate liability ledger?		
(b) How often balanced?		
E. CHARGED OFF ASSETS		
1. Are they segregated, properly controlled and frequently reviewed by Directors?		
2. Are records satisfactory?		

	Yes	No
F. DEPOSIT LIABILITIES		
1. (a) Are demand and savings ledgers periodically proved to the general ledger?		
(b) Frequency: Demand.....		
Savings.....		
2. Are proofs made of demand and savings ledgers at least quarterly by someone other than the deposit ledger bookkeeper?		
3. Are deposit ledger bookkeepers rotated?		
4. Are employees prohibited from both receiving deposits and posting ledgers? (Except on key controlled posting machine operations.)		
5. Are statements issued regularly (at least semiannually) on all checking accounts?		
6. Is a procedure in effect to prevent the payment of checks drawn against uncollected funds?		
7. Is master key to posting machine controlled and proof taken by person other than teller?		
8. Are savings accounts filed numerically?		
9. Are any savings passbooks held by the bank? If so, are they under the control of a designated officer?		
10. Are statements issued on non-passbook savings accounts? Frequency		
11. Are the following inactive (and/or dormant) accounts segregated and controlled?		
Checking accounts:		
Savings accounts		
12. (a) Do entries to dormant accounts require the approval of an officer?		
(b) If Yes, is this being enforced?		
G. OVERDRAFTS		
1. Is approval of an officer required?		
2. (a) Is adequate, permanent daily record maintained?		
(b) If Yes, is this record reviewed daily by the auditor or a designated officer?		
H. GENERAL LEDGER		
1. Are the general ledger and its subsidiary records satisfactory and sufficiently detailed?		
I. CERTIFICATES OF DEPOSIT, DRAFTS AND OFFICIAL CHECKS		
1. Are records satisfactory?		
2. Are they proved periodically and independently?		
3. Are forms pre-numbered?		
4. Are unused forms properly safeguarded?		
J. EARNINGS AND EXPENSES		
1. Is distribution of income and expense properly shown on bank's records?		
2. Is bank on either a partial or complete accrual system?		
(a) Does it appear to be properly operated?		
(b) Is a periodic check made by appropriate officers or employees of "Interest earned, not collected" and "Interest collected, not earned" for reconcilement?		
K. SAFEKEEPING		
1. Does bank accept items for safekeeping? If so,		
(a) Are satisfactory records maintained?		
(b) Are independent verifications made periodically?		
(c) Are proper receipts given and obtained?		
L. SAFE DEPOSIT BOXES		
1. Does bank maintain safe deposit box facilities? If so,		
(a) Does bank refuse to hold for renters any safe deposit box keys?		
(b) Is guard key to safe deposit boxes under bank's absolute control?		

INTERNAL CONTROLS (Continued)

ALL ANSWERS ARE YES UNLESS OTHERWISE NOTED

	Yes	No
L. SAFE DEPOSIT BOXES (Continued)		
(c) Are proper visitation records maintained?		
2. Are locks changed after each termination of lease?		
M. COLLECTIONS		
1. Are items segregated and controlled?		
2. Are satisfactory records maintained?		
N. CAPITAL STOCK		
1. Is satisfactory stock ledger maintained?		
2. Are surrendered certificates:		
(a) Properly assigned?		
(b) Properly cancelled?		
3. Are unissued certificates held in blank form until used?		
O. DIRECTORS AND DIRECTORS' COMMITTEE		
1. Are the following accounts frequently examined by the Board of Directors or a committee thereof:		
(a) Income and Expense accounts?		
(b) Over and short account?		
(c) Overdraft account?		
(d) Cash items and Suspense accounts?		
2. Is the bank's liquidity position reviewed and evaluated at least monthly?		
3. Do the minutes indicate action as noted under Nos. 1 and 2 above?		
4. Are the directors assisted by bank's (1) auditing staff, (2) rotated employees or (3) independent accountant in making directors' examinations? (Indicate by (1), (2), or (3) opposite answer)		

	Yes	No
O. DIRECTORS AND DIRECTORS' COMMITTEE (Continued)		
5. Does the examining committee:		
(a) Review and appraise the more important loans and discounts?		
(b) Review and appraise the investment account?		
(c) Review all types of insurance coverage?		
P. AUDITING DEPARTMENT		
1. Does the bank employ a full time auditor?		
2. If so, is he accountable only to the Board of Directors?		
3. Has a continuing program for the direct verification of loans and deposits been instituted by the Board of Directors?		
Q. AUTOMATION		
1. Give date of last E.D.P. report of examination.....		
(Form 1450 or 1555)		
2. Was the report reviewed by the directors and noted in the minutes?		
(a) Were internal controls satisfactory?		
R. MISCELLANEOUS		
1. Are all officers and employees required to be absent from the bank at least two consecutive weeks annually?		
2. Are unlocated differences periodically closed out through the general ledger?		
3. Are safeguards adequate for the handling of night deposits?		
4. Are unissued U. S. Savings Bonds and travelers checks kept under proper control?		

COMMENTS

BEST COPY AVAILABLE

IN THE UNITED STATES DISTRICT COURT

* * (Caption Nos. 71 C 454 and 71 C 1204) * *

AFFIDAVIT OF GERHARD MAYER

GERHARD MAYER, being duly sworn on oath, states as follows:

1. I have knowledge of the facts set forth below and will testify to such matters if called as a witness in the above captioned cases.

2. I am a certified public accountant and was engaged in the practice of public accounting for about thirty years until my retirement in 1969, since 1952 as partner in a firm of certified public accountants. As part of my duties in that capacity I kept myself informed about accounting and auditing rules, standards, and practices, and about applicable pronouncements and publications of professional organizations, especially the American Institute of Certified Public Accountants.

3. In making any audit, including that of a securities brokerage or dealer, it is important that the auditor be satisfied that no single employee, including an officer, has control of an entire transaction as well as of the documentation and records pertaining to it. Accordingly, standard instructions and practices of accounting firms as well as all authoritative pertinent pronouncements and publications require, as an integral part of auditing procedures, inquiry into so-called internal controls, including specifically investigation (i) whether there are established and followed adequate internal controls providing for segregation of duties so that no single member of the organization has control both of a transaction (such as receipt or delivery of cash or securities, or execution of notes or other evidences of indebtedness), and of the

recording of, and the records pertaining to, such transaction; and (ii), as a significant means of evaluating effectiveness of such internal control, as well as of the possibility of irregularities in transactions or recording, investigation whether duties of persons having control of assets or liabilities or records pertaining to them are rotated periodically, e.g., as result of regular vacations during which functions and responsibilities of vacationers carried out by other members of the organization.

Any significant failure of such investigation to yield an affirmative, independently verified answer would militate against issuing an accountants' report stating that the financial statements fairly present the financial condition of the organization being audited.

Failure to periodically make such investigation and evaluation would seem to constitute a significant departure from usual auditing standards.

4. If I had discovered in making an audit of a security brokerage business that its president had established an office rule that mail addressed to him at the business address, or to the company for his attention should not be opened by anyone but him, even in his absence; and that whenever he was away from the office such mail would remain unopened and pile up on his desk I would have to raise the question whether such rule or practice could possibly have been instituted for the purpose of preventing discovery of irregularities of whatever nature; would, as a minimum, have to undertake additional audit procedures to independently establish a negative answer to the latter question; also, failing such an answer either withdraw from the engagement or decline to express an opinion on the financial statements of the enterprise. I would do so for the reasons that (i) such a rule or prac-

tice is unusual and strange: and (ii) in a securities brokerage business the risk to the investing public from any irregularity is particularly severed in view of the fact that its capital usually is much smaller in relation to its liabilities than in most other lines of business.

/s/ Gerhard Mayer

State of Illinois)
) ss.
County of Cook)

Subscribed and sworn to
before me this 2nd day
of May, 1973.
/s/ Edith G. Anderson
Notary Public

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454 and 71 C 1204) * *

AFFIDAVIT OF FRED J. DUNCOMBE

FRED J. DUNCOMBE, duly sworn, on oath states as follows:

1. I have knowledge of the facts set forth below and will testify to such matters if called as a witness in the above captioned cases.

2. I am a Certified Public Accountant now retired from active practice. I graduated from Wisconsin State University in Whitewater, Wisconsin. I was employed as a Public Accountant by Haskins & Sells from 1920 to 1930. I was a Manager in its Chicago office in the late 1920s. I received my certificate as a Certified Public Accountant in the middle 1920s. I was a partner in the Public Accounting firm of George W. Rosetter & Company from 1930 to 1954 when that firm merged with the Public Accounting firm of Peat, Marwick, Mitchell & Co. and was a partner in the latter firm until my retirement in 1959. I was for three years a member of the Committee on Accountancy of the University of Illinois which directed the examinations for the degree of Certified Public Accountant in the State of Illinois, two of which years I served as Chairman of the Committee. I am a member of the Illinois Society of Certified Public Accountants and served as President of the Society in 1937.

3. I have had several years' experience in directing audits of brokerage firms. In auditing such firms it is important that the auditors be assured that no single employee has control of an entire transaction and of the documents and records of that transaction. Accordingly, the standard instructions of accounting firms making audits of brokerage firms require that the accountants actually making the audits of such firms investigate whether duties and responsibilities are clearly defined and unmistakably assigned in such a fashion that no single employee (a) has control of an entire operation and (b) has complete control over both transactions and the documents and records respecting these transactions.

4. If I had discovered in making an audit of a brokerage company that the President of the Company had established an office rule that all mail addressed to him or to the Company for his attention should not be opened by anyone but him; and that when he was away from the office for a few days, the mail addressed to him or to the Company for his attention piled up on his desk, I would not have regarded that brokerage firm as having adequate internal accounting control and would

not have certified that a report based on such an audit fairly represented the financial position of the Company.

/s/ Fred J. Duncombe

State Of Illinois)
) ss.
County Of Cook)

Subscribed And Sworn To
before me, a notary public,
this 27th day of April,
1973.
/s/ May A. Jackson
Notary Public

Ex 3 To Memorandum

SEC Rule 17a-5 (g, h, and i).

(g) Accountant's Certificate.

(1) Technical Requirements. The accountant's certificate shall be dated, shall be signed manually, and shall identify without detailed enumeration the items of the report covered by the certificate.

(2) Representations as to Audit. The accountant's certificate (A) shall contain a reasonably comprehensive statement as to the scope of the audit made, including a statement as to whether the accountant reviewed the procedures followed for safeguarding the securities of customers, and including, if with respect to significant items in the report covered by the certificate any auditing procedures generally recognized as normal have been omitted, a specific designation of such procedures and of the reasons for their omission; (B) shall state whether the audit was made in accordance with generally accepted auditing standards applicable in the circumstances; and (C) shall state whether the audit made omitted any procedure deemed necessary by the accountant under the circumstances of the particular case.

(3) Nothing in this rule shall be construed to imply authority for the omission of any procedure which independent accountants would ordinarily employ in the course of an audit made for the purpose of expressing the opinions required by paragraph (h) of this rule.

(h) Accountant's Certificate—Opinions To Be Expressed. The accountant's certificate shall state clearly the opinion of the accountant with respect to the financial statement covered by the certificate and the accounting principles and practices reflected therein.

(i) Accountant's Certificate—Exceptions. Any matters to which the accountant takes exception shall be clearly identified; the exception thereto shall be specifically and clearly stated; and to the extent practicable, the effect of each such exception on the related item of the report shall be given.

(Amended paras. (b)(1); Release 34-7100, dated Sept. 10, eff. Sept. 26, 1963; amended para. (b)(3), Oct. 3, Release 34-8177, eff. Nov. 30, 1967.)

BEST COPY AVAILABLE

CERTIFICATE

Willard L. King hereby certifies that on May 4, 1973 he caused a copy of the foregoing memorandum to be deposited in the United States mail, postage fully prepaid, addressed to:

Robert L. Berner, Jr.
Baker & McKenzie
700 Prudential Plaza
Chicago, Illinois

/s/ Willard L. King

IN THE UNITED STATES DISTRICT COURT

* * (Caption—No. 71 C 454) * *

Deposition of Jerry M. Hooker taken before Ruth L. Bernstein, C.S.R., Notary Public, pursuant to the provisions of the Civil Practice Act of the State of Illinois and the Rules of the Supreme Court thereof, pertaining to the taking of depositions for the purpose of discovery, at Suite 4105, 135 South LaSalle Street, Chicago, Illinois, commencing at 10:15 o'clock a.m. on the 24th day of August, A.D. 1971.

There were present at the taking of this deposition the following counsel:

King, Robin, Gale & Pillinger, by
Messrs. Willard L. King and Stanley N. Gore,
on behalf of the Plaintiffs;
Schiff, Hardin, Waite, Dorschel & Britton, by
Mr. Mitchell S. Rieger,
on behalf of Defendant Midwest Stock Exchange;
Baker & McKenzie, by
Messrs. Harry J. O'Kane and Robert L. Berner, Jr.,
on behalf of Defendant Ernst & Ernst.

Mr. King: This is the discovery deposition of the witness, Jerry Hooker, taken pursuant to agreement of the parties after notice, 10:15 in the morning.

JERRY M. HOOKER called as a witness herein, having been first duly sworn, was examined upon oral interrogatories and testified as follows:

Examination By Mr. King.

Q. Will you state your name for the record, Mr. Hooker?
A. Jerry M. Hooker.
Q. Where do you live?
A. 120 East Bradley Street, Des Plaines.
Q. What is your business or profession?
A. I am a CPA, a certified public accountant.
Q. How long have you been engaged in that profession?
A. Since 1957.
Q. What was your education?
A. I graduated from Northern Illinois University, bachelor's degree.
Q. In what year?
A. I got my certificate in 1958.
Q. With what accounting firm are you connected?
A. Ernst & Ernst.
Q. How long have you been connected with that firm?
A. Since 1957.
Q. What positions have you held with that firm?
A. Staff accountant, in—charge account, senior accountant, supervisor, manager and partner.
Q. How long have you been a partner?
A. Since October 1st, 1969.

Q. What has been your experience in auditing of brokerage firms?

A. I worked on audits of brokerage firms in all of the staff capacities that I just listed.

Q. Since what date?

A. Since the December 31st, 1957 audit of First Securities Company of Chicago.

Q. Have you audited any brokerage firms who were members of the New York Stock Exchange?

A. Only the branch offices of firms that are members, which are headquartered in New York.

Q. How many of those have you done?

A. Three.

Q. How many brokerage firms have you audited, which were members of the Midwest Stock Exchange?

A. Two.

Q. How long have you been a CPA?

A. Since 1962.

Q. Since the 1940's, the firm of Ernst & Ernst has audited the brokerage firm of First Securities Company of Chicago, isn't that true?

Mr. O'Kane: How would he know? He wasn't employed by them.

Mr. King: Let him say so if he doesn't know.

The Witness: A. I believe so.

Q. The firm was engaged to make that audit by Leston B. Nay, the president of First Securities Company, was it not?

Mr. O'Kane: What year are you talking about, sir?

Mr. King: Any year that he wishes to remember.

The Witness: A. Yes, sir.

Q. It was part of the engagement that the audit should be made for the Midwest Stock Exchange, isn't that true?

A. Yes; it was to be made to comply with the requirements of the Midwest Stock Exhcnage.

Q. Your firm did certain work for Leston B. Nay in addition to the audit of First Securities Company, did it not?

A. I can't recall now any additional work that we did do.

Q. Mrs. Alson, one of the plaintiffs in this case, testified that she paid First Securities Company for a study made by Ernst & Ernst of the tax consequences of her cashing up her insurance with the University of Chicago. Do you have any knowledge of that?

A. Yes. I believe that I recall seeing a letter that we issued on that, which was done by our tax department. I personally had nothing to do with that.

Q. I show you a letter from Ernst & Ernst to Leston B. Nay, president of the First Securities Company, dated February 6, 1948, which I will ask the reporter to mark Hooker Exhibit 1 for identification.

(Whereupon said exhibit was marked as requested.)

This letter states that Ernst & Ernst in connection with your audit of First Securities Company for the year ending December 31, 1947, has reviewed the company's system of internal accounting control, does it not?

A. Yes.

Q. This letter states in the next to the last paragraph on Page 2 that the essential of internal accounting control is a system which gives assurance that all transactions are recorded in the accounting record, does it not?

A. Yes.

Q. Do you agree with that statement, Mr. Hooker?

A. Yes.

Q. I show you a certificate of Ernst & Ernst addressed to the board of directors of First Securities Company of Chicago dated January 13, 1961.

Which I will ask the reporter to mark Hooker Exhibit 2 for identification.

(Whereupon said exhibit was marked as requested.)

Q. Ernst & Ernst certifies in this certificate that it has reviewed the system of internal accounting control of First Securities Company, does it not?

A. Yes, it does.

Q. Your firm certified that in view of that examination, the answers to the Financial Questionnaire fairly presented the financial position of First Securities Company, did it not?

A. Yes, it did.

Q. The answers to that questionnaire certified by you did not indicate that the company was insolvent, did they?

A. Would you repeat the question, please?

Mr. King: Would you read it to him, please?

(Whereupon the question was read as requested.)

A. No, they did not.

Q. The answers to that questionnaire indicated that the assets of First Securities exceeded its liabilities, did it not?

Mr. O'Kane: What questionnaire are you talking about?

Mr. King: (Indicating)

Mr. O'Kane: That is not a questionnaire.

Mr. King: The questionnaire is mentioned in the letter, which he holds.

Mr. O'Kane: If he knows.

The Witness: A. Do you have the questionnaire?

Mr. King: Q. No. I will come to it. I will come to later questionnaires.

Mr. O'Kane: Show it to him now.

Does that refresh your recollection?

The Witness: A. I will be able to answer your questions specifically about the questionnaire if I can see it.

This is not the same questionnaire.

Mr. King: No, it isn't.

A. This is 1964. This is a certificate relating to the 1960 questionnaire.

Q. That is correct. Now, can you answer my question?

Will you read him the question, please?

(Whereupon the question was read as requested.)

A. Do you have the 1960 questionnaire?

Q. No, I do not. I am referring to the questionnaire that was attached to Hooker Exhibit 2.

Mr. O'Kane: Mr. Hooker, would you know what it reflects, the questionnaire, without looking at it?

Mr. King: It is not your time to ask questions yet, sir.

Mr. O'Kane: I just want to clarify the record, sir.

Mr. King: When your time comes, you may do so.

The Witness: A. Yes, I believe the assets shown in the questionnaire exceeded the liabilities as shown on the 1960 questionnaire.

Q. Subsequent events have proved that that certification was not true and correct, have they not?

Mr. O'Kane: What subsequent events are you talking about, sir?

Mr. King: The witness knows; he may answer.

Mr. O'Kane: Knows about subsequent events? I am instructing him not to answer that question.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instruction?

Mr. O'Kane: That's right.

The Witness: A. Yes.

Mr. King: Q. Are you aware that claims have been filed against the estate of First Securities Company aggregating some $2,300,000 with assets in the estate of approximately $1,000,000?

A. I am aware that some claims have been filed. I wasn't aware of that amount.

Q. Were you aware that claims far in excess of the assets of the estate have been filed?

A. Yes.

Q. Are you aware that most of those claims existed at the date in January, 1961 when you made this certificate, which is Hooker Exhibit 2?

A. No.

Q. Are you aware that Nay's suicide note in 1968 stated that the company was bankrupt because of his thefts?

Mr. O'Kane: I object to that question unless you lay a proper foundation, if he knows of a suicide note.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: I am not instructing him not to answer. I want some clarification.

Mr. King: Q. Are you refusing to answer counsel's question?

Mr. O'Kane: In the present form. He can't understand it.

The Witness: A. I have not seen the suicide note.

Mr. King: Q. How do you explain the failure of Ernst & Ernst to discover Nay's thefts?

Mr. O'Kane: I object to that question.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: Absolutely. It is a conclusion for the fact finder of the law based upon all the salient facts in this case.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Are you aware that in his suicide note, Nay asked that Ernst & Ernst be notified of his thefts?

Mr. O'Kane: He just indcated to you that he didn't read it.

Mr. King: You may instruct him not to answer.

Mr. O'Kane: I instruct him not to answer anything but—the man indicated he didn't read the suicide note so how can he testify as to its contents?

The Witness: A. I have not read the suicide note that you have referred to.

Mr. King: Q. Have you heard it discussed?

A. I read about it in the newspapers.

Q. Were you aware that Nay asked in his suicide note that Ernst & Ernst be notified of his thefts?

A. No, I wasn't aware of that.

Q. You stated in Hooker Exhibit 2 that you had reviewed the system of internal accounting control of First Securities, did you not?

A. Yes.

Q. Will you tell us what was done on that review?

A. Our review consisted of testing the recorded transactions by the company, and reviewing the procedures that they followed. We tested those procedures. We tested the reliability of the accounting records by examining outside documentation, confirmations with customers, brokers, and transfer agents and inquiry and dis-

cussions with the officers of the company. Certainly an audit, a completed audit, is to some extent a review and a test of the internal controls of a company.

Q. Have you completed your answer?

A. Yes.

Q. The Financial Questionnaire referred to in Hooker Exhibit 2 is the printed or typed questionnaire of the Midwest Stock Exchange, is it not?

A. Would you read that question?

Mr. King: Will you read it to him, please?

(Whereupon the question was read as requested.)

A. This Exhibit 2 refers to the answers to the questionnaire, which is in response to the printed questionnaire, yes, by the Midwest Stock Exchange.

Q. It is substantially the same questionnaire of the New York Stock Exchange, isn't it?

A. I believe so.

Q. And it is substantially the questionnaire prescribed by the S.E.C., isn't that true?

A. That is true.

Q. I show you a certificate of Ernst & Ernst to the board of directors of First Securities Company dated January 12, 1962.

Which I will ask the reporter to mark Hooker Exhibit 3 for identification.

(Whereupon said exhibit was marked as requested.)

In this certificate, your firm again certified that it had examined the system of internal accounting control of First Securities Company, did it not?

A. Yes.

Mr. Berner: Excuse me, Mr. King. May I see it?

Mr. King: Indeed.

Mr. Berner: I didn't understand what the question was that they certified and examined the system.

May I hear Mr. King's last question, please?

(Whereupon the question was read as requested.)

Mr. King: Ernst & Ernst stated in this Hooker Exhibit that their report to the Midwest Stock Exchange will state that their examination included a review of the system of internal accounting control, does it not?

The Witness: A. I am sorry. Would you repeat that question?

(Whereupon the question was read as requested.)

Mr. King: I will withdraw that question.

Q. I show you a letter dated January 9, 1963 from Ernst & Ernst to First Securities Company, which I will ask the reporter to mark Hooker Exhibit 4 for identification.

(Whereupon said exhibit was marked as requested.)

By this letter, Ernst & Ernst accepts the appointment as independent accountant of First Securities Company for the year 1963 for a surprise audit as required by the rules of the Midwest Stock Exchange, does it not?

A. Yes.

Q. Ernst & Ernst stated that their report to the Midwest Stock Exchange will state that their examination included a review of the system of internal accounting control of First Securities Company, does it not?

A. It says that our examination will include that, but it doesn't say our report to the Midwest Stock Exchange.

Q. I call your attention to the next to the last sentence, "our report will include."

A. Yes. Our report will include a review of the system of internal control and the procedures for safeguarding securities.

Q. That is contained in the letter, is it not, what you have just said?

A. Yes.

Q. A copy of Hooker Exhibit 4 was sent to the Midwest Stock Exchange, was it not?

A. Yes.

Q. I show you a letter dated January 11, 1963 from Ernst & Ernst to the board of directors of First Securities Company.

Which I will ask the reporter to mark Hooker Exhibit 5 for identification.

(Whereupon said exhibit was marked as requested.)

In this letter, Ernst & Ernst states that its audit will include a review of the system of internal accounting control of First Securities Company, does it not?

A. Yes.

Q. I show you a letter from Ernst & Ernst dated September 13, 1963 to the board of directors of First Securities Company.

Which I will ask the reporter to mark Hooker Exhibit 6 for identification.

(Whereupon said exhibit was marked as requested.)

In this letter, Ernst & Ernst states that the company answers to the Financial Questionnaire fairly state the financial position of First Securities Company, does it not?

A. Yes.

Q. Subsequent events have proved that that statement was not true and correct, have they not?

Mr. O'Kane: That is an assumption on the part of counsel, not based on fact, which even if it was based on fact, he wouldn't have any knowledge.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Hooker Exhibit 6 also states that Ernst & Ernst have reviewed the system of internal control of the accounts of First Securities Company, does it not?

A. Yes.

Q. I show you a letter dated January 16, 1964 from Ernst & Ernst to the Midwest Stock Exchange, which I will ask the reporter to mark Hooker Exhibit 7 for identification.

(Whereupon said exhibit was marked as requested.)

Ernst & Ernst in this letter notified the stock exchange that it had accepted the appointment as the independent accountant of First Securities Company for the year 1964, does it not?

A. Yes.

Q. It states that it understands the stock exchange will mail to First Securities Company, the instructional forms for the Financial Questionnaire, does it not?

A. Yes.

Q. Attached to this letter is a letter from Ernst & Ernst to First Securities Company with a copy to the Midwest Stock Exchange accepting the appointment as independent accountant, does it not?

A. Yes.

Q. This letter states, and I quote: "Our report will state that our examination included a review of the system of internal control," does it not?

A. Yes.

Q. I hand you a document entitled "Answers to Financial Questionnaire, September 30, 1964, consisting of ten pages.

Which I will ask the reporter to mark Hooker Exhibit 8 for identification.

(Whereupon said exhibit was marked as requested.)

The third page of Hooker Exhibit 8 is the accountant's certificate of Ernst & Ernst dated October 9, 1964.

Mr. O'Kane: Excuse me. That is an accountant's report, third page.

Mr. King: Please don't coach the witness.

Mr. O'Kane: I am not coaching the witness. You are calling it a certification. If you are referring to Page 3, then you must have some other page in mind. Page 3 is a document that we have captioned "Document Report."

Mr. King: I submit that the witness should do the testifying, not counsel.

Will you read him the question?

(Whereupon the question was read as requested.)

Mr. King: Q. Is it not?

The Witness: A. No. It is marked "Accountant's Report."

Q. This report states that Ernst & Ernst has reviewed the system of internal accounting control of First Securities Company, does it not?

A. Yes.

Q. It states that the accompanying answers to Financial Questionnaire present fairly the financial position of First Securities Company of Chicago, does it not?

A. Yes.

Q. Subsequent events have proved that that statement was not true and correct to your knowledge, have they not?

Mr. O'Kane: Objection. It is a conclusion you made, not a conclusion that the witnss can. It invades the province of the fact finder.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. The sixth sheet of Hooker Exhibit 8 shows some forty-eight thousand due to the company from an officer and former employee, does it not?

A. Yes.

Q. Can you tell us what this is, Mr. Hooker?

A. This is a receivable by the company from an officer and former employee in the amount of approximately $48,000.

Q. Do you know who the officer was?

A. Yes. The officer was Mr. Nay.

Q. The last sheet of Hooker Exhibit 8 bears your name at the top, does it not?

A. Yes, it does.

Q. Is that in your handwriting?

A. Yes, it is.

Q. This sheet indicates that your audit of First Securities Company extended over a period of five days, does it not?

A. No, it does not.

Q. How many days did it extend over?

A. You can't tell from this sheet. This sheet is what we call a calendar, which sets forth the item that should be done on each of these days. In addition, there are

other procedures that are performed after those five days. You will note down there at the bottom where it says: "Mail, second request." That is usually at least a week to ten days after the date of the audit.

Q. Before each paragraph on Hooker Exhibit 8, there is a date, is there not?

A. Yes, there is.

Q. And adding those dates, they amount to five days, do they not?

A. Five days or a span of five days?

Q. The sheet indicates that your audit extended over a period of five days, does it not?

A. No, it does not.

Q. How do you account for the fact that there are five dates shown on your agenda sheet?

A. As I explained, under each date, there are certain procedures that we want to perform on that date. In addition to these days, we have other procedures that can be performed, must be performed, but they don't have to be done at a certain time, but this sheet does not indicate that the audit was performed in five days or during the five day period.

Q. Now, can you tell us how many days the audit did take?

A. I can't tell you exactly, but I can approximate that it would have taken approximately ten working days.

Q. The sheet indicates that on three separate days, you examined and listed the incoming mail of First Securities Company, does it not?

A. Yes, it does.

Q. It is standard accounting procedure of an auditing brokerage firm to examine the incoming mail and list it, is it not?

A. It is standard procedure to examine the incoming mail and to list the securities that are received for a few days after the date of the audit.

Q. You examined the incoming mail in this way each year that you made the audit, did you not?

A. Yes, we did.

Q. Am I wrong in calling that an agenda for the audit, referring to the last sheet of Hooker Exhibit 8?

A. I think you would be wrong. You would have to define agenda as you are using it here.

Q. Well, this is a statement presented before you went to the audit, indicating what you intended to do on specific days, is it not?

A. Yes, it is.

Q. Each year this agenda indicates that you proposed to examine and list the incoming mail on three successive days, does it not?

Mr. O'Kane: This agenda, you are talking about?

The Witness: A. Well, this agenda, as you call it, which we call the calendar, is only for 1964.

Mr. King: Q. But there was a similar agenda for each year when you made an audit, was there not?

A. I wasn't involved in all of the audits that were made.

Q. Well, each year that you were involved, you had a sheet like the last sheet of Hooker Exhibit 8, indicating what you intended to do, isn't that true?

A. We had a sheet that was similar to this, as I recall.

Q. During the years you were making the audits, can you tell us what the charge of Ernst & Ernst was with the audit?

A. I can tell you approximately.

Q. That is all I want.

A. I think that at least for several of the years, our fee was approximately two thousand dollars to twenty-five hundred dollars, I believe.

Q. I show you a document which I will ask the reporter to mark Hooker Exhibit 8A for identification, consisting of three pages.

(Whereupon said document was marked as requested.)

What is this, Mr. Hooker?

A. This document?

Q. Yes.

A. The first page is what we call the 1962 calendar. The second page is a listing of incoming mail, where I had listed the securities received from the transfer agent.

Q. Now, on that, Mr. Hooker, did you examine all of the incoming mail and list only the mail that had securities in it?

A. Well, we were present when they opened the mail, and they sorted the mail down into the company mail and the mail for individuals. The company mail that was opened, if it included any securitiess, we listed those securities.

Q. You insisted on the company mail being opened in your presence?

A. Yes.

Q. Isn't this true?

A. That is true on that day.

Q. And you listed from that mail the incoming securities?

A. Yes.

Q. The second sheet of this exhibit has the words "John M. Jackson, trustee." What is the significance of that, Mr. Hooker?

A. Securities were received from the transfer agent, Banker's Trust Company. The securities received were Futterman Corporation, Class A, and there were 2,218 shares in the name of John M. Jackson, trustee.

Q. Are you aware that on Nay's suicide, voluminous correspondence was found in the office of First Securities Company with John M. Jackson relating to his investment of $226,000 in a fictitious escrow?

A. No, I am not.

Q. You never saw any of that correspondence during your audit?

A. No.

Q. Isn't that true?

A. That is true.

Mr. Rieger: I want to have the reporter read the name.

(Whereupon the name was read as requested.)

Mr. King: Q. The third sheet of Hooker Exhibit 8A is the five line memorandum of your review of the internal accounting control system of First Securities Company, is it not?

A. It is.

Q. That is in your handwriting, is it not?

A. It is not.

Q. Will you please read to us the last two lines of this memorandum?

A. "Based on our review, we feel that our audit program adequately reflects the company's procedures as of 12/31/62."

Q. Subsequent events have proved that your review of the company's internal accounting control system was not adequate, have they not?

A. No, they have not, to my knowledge.

Q. I show you a document, which I will ask the reporter to mark Hooker Exhibit 8B for identification.

(Whereupon said exhibit was marked as requested.)

Mr. Rieger: Off the record.

(Whereupon a discussion ensued off the record.)

Mr. King: Consisting of six pages.

(Whereupon said exhibit was marked as requested.)

On the second sheet of this exhibit appears the name Olga Hochfelder. Do you know who Olga Hochfelder was?

A. Based on this sheet, I would say that she was a customer of First Securities Company.

Q. This entry on your record shows that on January 5, 1962, First Securities Company received from Chase Manhattan Bank fifty shares of Class A stock of Crater Corporation in the name of Olga Hochfelder, does it not?

A. I can't tell if it is fifty shares or a hundred fifty shares.

Q. But it does show the shares received in the name of Olga Hochfelder?

A. Yes.

Q. Are you aware that the voluminous correspondence with Olga Hochfelder found in the office of First Securities Company after Nay's death shows that that company sold these fifty shares of stock in the Crater Corporation so that Miss Hochfelder could invest in a fictitious escrow?

A. No.

Q. I show you a document consisting of two pages, dated December 21, 1964, being a letter from Ernst & Ernst to the Midwest Stock Exchange, which I will ask the reporter to mark Hooker Exhibit 9 for identification.

(Whereupon said exhibit was marked as requested.)

By this letter Ernst & Ernst accepts the appointment as independent accountant of First Securities Company for the year 1965, does it not?

A. Yes.

Q. You enclosed with this letter a copy of the letter of December 21, 1964 to First Securities Company, agreeing to accept the appointment for surprise audit for the calendar year 1965, which is the second sheet of Hooker Exhibit 9, did you not?

A. Yes.

Q. Is this letter, Ernst & Ernst agrees that its report will state that its examination will include a review of the system of internal accounting control of First Securities Company, does it not?

A. Yes.

Q. I show you a letter from Ernst & Ernst to First Securities Company, dated May 17, 1965, which I will ask the reporter to mark Hooker Exhibit 10 for identification.

(Whereupon said exhibit was marked as requested.)

This is the certificate of Ernst & Ernst on its audit of April 30, 1965, is it not?

A. It is the accountant's report.

Q. This report certifies that your audit included a review of the system of internal accounting control of the accounts, does it not?

A. The report states that our examination included a review of the system of internal control.

Q. I show you a document consisting of twenty pages, which I will ask the reporter to mark Hooker Exhibit 11 for identification.

(Whereupon said exhibit was marked as requested.)

What is this, Mr. Hooker?

A. This is what we refer to as our audit program.

Q. Will you please look at the last page. Is that the program detailed agenda for your audit of April 10, 1965?

A. For what date was that?

Q. April 30, 1965. I misspoke.

A. This is our calendar for that audit.

Q. Does the last page of this bear your initials?

A. Yes, it does.

Q. Who prepared this report, which is Hooker Exhibit 11?

A. One of the men on our staff prepared this under my supervision.

Q. Do you know his name?

A. I believe that it was Jim Carr. I should add also that this particular one was, but that we have had write ups of the company's procedures, which are updated and who initially prepared that write up, I don't know.

Q. In other words, this was prepared from a prior write up of the proposed procedures on the audit?

A. Yes, sir.

Q. Please turn to the page numbered 12 of this report. Please note the words: "Vacations are taken regularly by all employees, and the duties of the employees are assumed by others in their absence." Do you find those words?

A. Yes, I do.

Q. What is the significance of that?

A. This is an element of internal control that all employees take vacations, and their duties are assumed by others, so that they can carry on the business of the company.

Q. Did the instructions of Ernst & Ernst to its accountants making this audit require them to make this inquiry regarding vacations?

A. No, we didn't have any instructions that require you make inquiry.

Q. Did your instructions contain any question comparable to the question which I find in the typed instructions of another internationally known auditing firm making brokerage audits: "Are all employees required to take a vacation at least annually"?

A. Would you read that question?

Mr. King: Read it, please.

(Whereupon the question was read as requested.)

A. I can't say that our instructions included that question although it is a typical question that would be asked.

Q. Did you ask who took over the duties of employees on vacations?

A. Are you referring to this audit?

Q. Yes.

A. I don't know if that question was asked or not.

Q. Is there a record of any inquiry about vacations in your working papers?

A. I don't know.

Q. It is standard auditing practice to inquire whether employees take regular vacations, is it not?

A. Yes.

Q. Do you recall of whom you made those inquiries in this audit?

A. I would not have made the inquiries in this audit. I was the supervisor on the audit, which means that I would have reviewed the work after it would have been completed. The senior on the audit was James

Carr, and I believe he would have directed the questions to Roy Campbell, who is the cashier.

Q. If an employee failed for several years to take any vacation, that would be a red flag of warning to the auditors, would it not?

A. It could be.

Q. Do you know whether any inquiry was made on whether Leston B. Nay, the president of the company, had taken regular vacations?

A. I don't know.

Q. If you had made an inquiry and discovered that he did not take regular vacations, that would have been a red flag of warning, would it not?

Mr. O'Kane: I am going to object to that. First of all, he wouldn't have made the inquiry. You are asking him for something outside of his knowledge.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: Sure. He can answer questions only based on his knowledge.

Mr. King: Q. Are you refusing to answer based on your counsel's instructions?

The Witness: A. Yes.

Q. Do you customarily ask to see the vacation schedule in a brokerage audit?

A. I don't believe we customarily ask to see the vacation schedule although we have to inquire about vacations as when we are doing the audit on a surprise basis, to schedule our surprise audit at a time when the key people are there.

Q. You merely ask the officer manager if the employees take regular vacations, and he says, yes, isn't that true?

A. Generally, that coupled with what I just said about scheduling our audit.

Q. Shouldn't you ask more than one person in the office if there is anyone who does not take regular vacations?

Mr. O'Kane: I object to that. That is a conclusion which you draw.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Right.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

A. Yes.

Q. I call your attention to the sheet marked 14 of Hooker Exhibit 11. This sheet states that your audit is to include a review of the system of internal accounting control, does it not?

A. Yes.

Q. I show you a letter dated December 23, 1965 from Ernst & Ernst to First Securities Company, which I will ask the reporter to mark Hooker Exhibit 12 for identification.

(Whereupon said exhibit was marked as requested.)

In this letter, Ernst & Ernst accepts the appointment as independent accountant at First Securities Company for the year 1966 as required by the Midwest Stock Exchange, does it not?

A. Yes.

Q. Ernst & Ernst agrees to notify the Midwest Stock Exchange on the date it commences its audit, does it not?

A. To notify them as of the date we commence our audit.

Q. This like your other audit was to be a surprise audit, was it not?

A. Yes.

Q. This letter states that your report to the Midwest Stock Exchange will state that your examination included a review of the system of internal accounting control of First Securities Company, does it not?

A. Yes.

Q. I show you a document of twenty pages, which I will ask the reporter to mark Hooker Exhibit 13 for identification.

(Whereupon said exhibit was marked as requested.)

These are the audit papers taken from your working papers for the Ernst & Ernst audit of First Securities Company of September 30, 1966, are they not?

A. Would you read that question back, please?

(Whereupon said question was read as requested.)

Well, it includes copies of our working papers from the September 30, '66 audit as well as the October 31st, '67 audit.

Q. The papers have been altered in ink to be copied into your 1967 audit, isn't that true?

A. They have been changed. I can't tell if they were altered in ink or not.

Q. The second sheet of Hooker Exhibit 13 is a letter by Ernst & Ernst to the board of directors at First Securities Company, dated October 17, 1966, containing the undertaking of Ernst & Ernst that they have reviewed the internal accounting control of First Securities Company, and that the accompanying answers to financial questionnaires in their opinion fairly represent the financial position of the First Securities Company as of September 30, 1966, does it not?

A. Well, not exactly. It says that the accompanying financial questionnaire presents fairly the financial position of First Securities Company of Chicago as of September 30, 1966.

Q. Subsequent events have proved that this last statement was not true or correct, have they not?

A. Not to my knowledge, they have not.

Q. The fourth sheet of Hooker Exhibit 13 shows the amount due from an officer as $54,132.96, does it not?

A. Yes, it does.

Q. That officer was Leston B. Nay, was it not?

A. Yes, it was.

Q. I show you a document dated October 31, 1967, which I will ask the reporter to mark Hooker Exhibit 14 for identification.

(Whereupon said exhibit was marked as requested.)

What is this, Mr. Hooker?

A. This is the answers to the financial questionnaire as of October 31st, 1967 for First Securities Company of Chicago.

Q. This is a duplicate of the original, is it not?

Mr. O'Kane: If you know.

The Witness: A. Let's say it is a conforming copy. I wouldn't call it a duplicate of the original.

Mr. King: Q. Again your signed certificate states that you have reviewed the system of internal accounting control, and that in your opinion, the answers to the questionnaire fairly present the financial situation of First Securities Company as of October 31, 1967, does it not?

A. Well, not the financial situation. The financial position, it does.

Q. Subsequent events have demonstrated that that statement was not true and correct, have they not?

A. No, not to my knowledge.

Q. I notice that on this exhibit for the first time, Ernst & Ernst certified to the Midwest Stock Exchange, and I quote: "We hereby attest that the above mentioned audit was made by us, and that the regulations for audit prescribed by the exchange were complied with in all particulars, isn't that true?

A. Yes.

Q. Did the regulations for audits of the Midwest Stock Exchange contain any regulations whatever relating to the internal accounting control?

Mr. O'Kane: May I have that question read back, please?

(Whereupon said question was read as requested.)

The Witness: A. I would like to read the regulations for audits again before I answer that, if I may.

Mr. King: Q. Well, it is nine pages long. It will take you a little bit.

Mr. O'Kane: Are you now asking the witness whether or not this document, the financial questionnaire to Midwest Stock Exchange, contains any information relating to internal control?

Mr. King: I stand on my question.

Mr. O'Kane: Read the question back, please.

(Whereupon the question was read as requested.)

The Witness: A. Yes.

Mr. O'Kane: The document speaks for itself. We are not going to read nine pages of documents. You can read them as well as he can. They are right here on Page 8 under the caption, "audit requirements."

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: I am instructing the witness not to read.

Mr. King: Q. Do you refuse to answer in accordance with your counsel's instructions?

The Witness: A. Yes.

Q. If you had discovered on your audits of First Securities Company that Nay, the president, took no vacations and had established an office rule that all mail addressed to the company for his attention should not be opened by anyone but him, would you have approved its system of internal accounting control?

Mr. O'Kane: I object to that question. That is two questions in one.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Not an answer to a double question. You can ask him singly. He will answer every single question you hive to interrogate this man on.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. The company had no internal accounting control whatever under the circumstances recited in my last question, isn't that true?

Mr. O'Kane: Do you know what he means by internal control as used in that question?

Mr. King: It is not your turn to question the witness. You may instruct him not to answer if you wish.

The Witness: Would you repeat the question, please?

Mr. King: Read it back.

(Whereupon the question was read as requested.)

The Witness: A. I don't know what you mean by that question.

Q. You are wholly unable to answer the question, isn't that true?

A. Well, I don't know because I don't know what you mean by it.

Q. You know what internal accounting control means, do you not?

A. Yes.

Q. My question was: Did the company have any internal accounting control whatever under the circumstances recited in my question? Would you like to have the question read?

A. No. I understand what you said, but the company did have accounting internal control.

Q. Adequate internal accounting control includes the requirement that transactions be handled by more than one person, isn't that true?

A. Generally, yes.

Q. Did Ernst & Ernst have a set of typed instructions to its accountants making an audit of a brokerage house?

A. Well, we didn't have instructions per se, but we did have a questionnaire that we completed.

Q. That was prepared by Ernst & Ernst?

A. Yes.

Q. Correct?

A. Yes.

Q. Did that questionnaire contain a question comparable to the following, which I find in the typed instructions of another national auditing firm to its accountants making an audit of a brokerage house: "Are duties and responsibilities clearly defined and unmistakably assigned in such a fashion that no single employee (a) has control of entire operation. (b) has complete control over both transactions, documents and the records controlling those transactions?"

A. I don't recall if our questionnaire would have included that question although this is a typical question

that is asked in connection with the review of the internal controls.

Q. You regard that as a proper instruction to the accountants making an audit of a brokerage house, do you not?

A. Yes.

Q. Do you recall that the Federal Insurance Company which wrote the brokers' blanket bond of First Securities Company, at one time refused to renew the bond unless the bank account reconciliations were made by someone other than the person who handled the cash?

A. Yes, I believe I knew that that was their requirement.

Q. I show you a letter dated May 26, 1961 from Federal Insurance Company refusing to renew the brokers' blanket bond unless some other person than the cashier made the reconciliation of the bank account, which I will ask the reporter to mark Hooker Exhibit 15 for identification.

(Whereupon the said exhibit was marked as requested.)

As a result of this letter, Ernst & Ernst told Nay that he would have to have someone other than the cashier reconcile the monthly bank statements, did they not?

A. Would you read the question again, please?

(Whereupon the question was read as requested.)

I don't recall Ernst & Ernst saying that they would have to do that.

Q. I show you a letter dated August 22, 1961 from Nay to Ernst & Ernst, which I will ask the reporter to mark Hooker Exhibit 16 for identification.

(Whereupon said exhibit was marked as requested.)

Will you please read into the record the first paragraph of this letter?

A. "Referring to our recent conversations with respect to the strengthening of our internal controls, be advised that beginning with the month of September, Mrs. Ryan will reconcile our bank statements monthly."

Q. Are you aware that after Nay's suicide, the insurance company on this brokers' blanket bond paid the receiver of First Securities Company $100,000, the full amount of the bond because of Nay's defalcations?

A. No.

Q. If the insurance company had known that Nay did not take vacations and would not permit anyone in the office to open mail addressed to the company for Nay's attention, it would have refused to write that bond just as it refused to write it unless someone other than the cashier reconciled the bank statement, isn't that true?

Mr. O'Kane: How would he know? He is not an expert in insurance bonding.

Mr. King: Please don't coach the witness.

Mr. O'Kane: I am objecting to the question.

Mr. King: Do you instruct him not to answer?

Mr. O'Kane: Sure.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Are you aware that during these years that you were auditing the account at First Securities Company, Nay had a large number of transactions in which he persuaded a customer of the company to sell his standard securities and put the proceeds in a fictitious escrow, embezzling the money himself?

A. I have read about that in the newspaper and the complaint. That is the only knowledge I have of it.

Q. Are you aware that Nay had a large correspondence on the letterhead of First Securities Company with these fititious escrow victims, which he kept locked in a drawer of a desk at First Securities Company, so that transactions would not appear on the books of the company?

A. I have not seen any of that correspondence.

Q. First Securities Company was a member of the National Association of Security Dealers, was it not?

A. Yes.

Q. Are you acquainted with Rule 27C of the NASD?

A. Which rule is that?

Q. I show you a printed copy of that rule.

A. Yes, sir.

Q. Does not that rule require a member to endorse in writing on an internal record all correspondence of its registered representatives pertaining to the solicitation or execution of any securities transactions?

A. I believe that is a legal question that I am not qualified to answer.

Q. What is the purpose of this Rule 27C?

Mr. O'Kane: I object to that as a leading conclusion. He is not a lawyer.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Was not that rule adopted by the NASD and approved by the SEC for the very purpose of preventing Nay's procedure in this case of holding out correspondence from the company records?

Mr. O'Kane: Same objection.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Did First Securities Company make any effort to your knowledge to comply with Rule 27C of the NASD?

Mr. O'Kane: Objection. That question also calls for a legal conclusion. He is not an expert in the field.

Mr. King: Do you instruct the witness not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Did you make any effort to check in your audits whether First Securities Company complied with NASD Rule 27C?

Mr. O'Kane: Same objection.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

A. Yes.

Q. Did First Securities Company keep any records of its correspondence?

A. Yes, sir.

Q. Did you ask anyone at First Securities why it ignored NASD Rule 27C?

Mr. O'Kane: Objection; same thing.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: Yes, sir.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Were you or anyone from Ernst & Ernst aware of Nay's office rule that all mail addressed to the company for his attention should be opened by no one but Nay?

Mr. O'Kane: I object to that question on the ground that whatever was in Lester B. Nay's direction to any of his employees would not necessarily be known by this defendant or any of its representatives. If you want to phrase the question as to what he knew if anything were Mr. Nay's instructions, I would let him answer that question.

Mr. King: That was exactly the way I did have the question.

Would you read the question to the witness?

(Whereupon said question was read as requested.)

Mr. King: Do you stand on your objection?

Mr. O'Kane: Right.

Q. Are you instructing the witness not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Would you have approved that rule if you had been aware of it?

A. I would not take any objection to the rule.

Q. Did you make any inquiries about who customarily opened the mail?

A. Yes.

Q. Whom did you ask?

A. Generally, Roy Campbell who is the cashier and also, we observed the opening of the mail.

Q. How could you certify that there was proper internal accounting control when letters from customers of the company could be opened by no one but Nay?

Mr. O'Kane: Objection to that question. It is a conclusion of fact and goes to the ultimate issue in this lawsuit.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Yes, sir.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Would not the knowledge of that office rule have aroused your suspicions in any way?

A. No.

Q. Isn't the opening of mail vital to internal accounting control?

A. No.

Q. Since Nay's suicide, have you made any audits of brokerage firms?

A. Yes.

Q. Have you in those cases inquired as to who opened the mail?

A. Yes.

Q. If today you discovered in a brokerage audit that only one person opened the mail and that person never took vacations, would you certify that there was proper internal accounting control?

Mr. O'Kane: I will object to the question based upon what he would do today. That is not an issue in this case.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: That's right.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Your audit of September 30, 1966, which is Hooker Exhibit 13, shows that Nay had borrowed from the company $54,931.73, does it not?

A. What was the amount again?

Q. $54,931.73.

A. No, sir. No, that is not the amount that Nay had borrowed.

Q. What is it?

A. The amount was $54,132.96, the one with the red arrow.

Q. It shows that Nay had borrowed $54,931—$54,132.96, does it not?

A. Yes.

Q. Your audit of October 31, 1967, which is Hooker Exhibit 14, shows that Nay had borrowed from the company $84,436.72, does it not?

A. Yes.

Q. The issued capital stock of the company amounted to $30,000, isn't that true?

A. Yes.

Q. Was it not extraordinary for the president of the company to borrow from the company almost three times the amount of its issued capital stock?

A. I don't know if you would say it was extraordinary.

Q. Have you ever in your experience in brokerage auditing known the president of a company to borrow so heavy a proportion of the company's capital?

A. I don't believe so.

Q. Didn't this situation impose some further duties upon Ernst & Ernst as auditors?

A. Further beyond what?

Q. Beyond the duties that you did.

A. Not that I am aware of.

Q. I show you a memorandum in your files, which I will ask the reporter to mark Hooker Exhibit 17 for identification.

(Whereupon said exhibit was marked as requested.)

Whose handwriting is this?

A. Mine.

Q. You indicate in this memorandum that you call the attention of the Stock Exchange to the fact that because of Nay's borrowing, the capital of First Securities was impaired below the minimum requirements of the Stock Exchange, did you not?

A. This memorandum doesn't say that.

Q. Will you read the first sentence of the memorandum?

A. "As of October 31st, 1967, the company did not meet the minimum capital requirements of the Midwest Stock Exchange by approximately $9,000." It doesn't state the reason for the deficiency.

Q. What were the minimum requirements of the Exchange?

A. $25,000 net capital is defined plus the ratio of the aggregate indebtedness of capital twenty to one.

Q. Mr. Rothing on behalf of the Exchange told you that the impairment had been corrected by Nay's paying $10,000 on his $84,000 indebtedness to the company, did he not?

A. This memorandum doesn't say that.

Q. But isn't that the fact, to your knowledge?

A. I can't recall if that is what Mr. Rothing said.

Q. I show you a letter dated November 13, 1967 from Nay to the Midwest Stock Exchange, stating that "I

have this day reduced my indebtedness to the company," meaning First Securities Company, "represented by an installment note in the sum of $10,000 and thereby have effected a return to full compliance with your net capital rule." Does that letter refresh your recollection?

Mr. O'Kane: As to what?

Mr. King: As to whether Nay remedied the deficiency by paying $10,000.

The Witness: A. This letter says that he paid $10,000.

Q. On that date, does it not?

A. On November 10th—no, wait a minute. "I have this day"—yes, November 13, paid $10,000.

Q. Were you aware that in the following April, Nay borrowed an additional $30,000 from the company?

A. April of 1968?

Q. Yes.

A. That October, 1967 was the last audit that was performed.

Q. You are quite right.

A. No, I was not aware of the additional transaction.

Mr. Rieger: Could I have the amount reread, an additional how much?

Mr. King: $30,000.

Q. Your memorandum, which is Hooker Exhibit 17 states, and I quote: "Mr. Rothing said that if a company had a deficiency in its capital account which was not corrected within a reasonable time, the Exchange would suspend the company from trading," does it not?

A. Yes.

Q. Did Mr. Rothing indicate what was the reasonable time for a broker to correct a deficiency in its capital below the minimum requirements of the Exchange?

A. I don't recall.

Mr. King: Well, gentlemen, it is twelve o'clock. I have about an hour more. I can go on for an hour or I can recess.

What about you, Miss Reporter?

The Reporter: I can continue.

Mr. King: Q. Did the questionnaire that Ernst & Ernst received from the Midwest Stock Exchange for this audit, contain any requests that the auditors ascertain whether the employees and officers of the firm took regular vacations? Do you want it to be read?

The Witness: A. No. I think I understand the question. I don't recall if the questionnaire included instructions on that.

Q. Did the questionnaire or instructions that Ernst & Ernst received from the Midwest Stock Exchange for this audit, contain any request that the auditors ascertain whether the employees and officers had their duties performed by some other person when they were on vacation?

Mr. O'Kane: At what time?

Mr. King: At the time he received the questionnaire.

Mr. O'Kane: This questionnaire you handed him is dated February 20, 1970.

Mr. King: It is identical with the prior question.

Mr. O'Kane: We don't know that so he can't very well answer something he doesn't know.

Do you know what is in the previous financial questionnaire? That is what he is asking you.

The Witness: A. I don't recall what was in there.

Mr. King: Q. Did the instructions that Ernst & Ernst received from the Midwest Stock Exchange for this audit contain any requests that the auditors ascertain who opened the mail received by the company and whether that person took regular annual vacations?

A. I don't recall anything in the instructions relating to that.

Q. Did the questionnaire received from the Midwest Stock Exchange contain any requests that the auditors for this audit ascertain whether or not the company had a rule that mail addressed to the company for the attention of any officer could not be opened by anyone but him so that when he was away, the mail piled up on his desk?

A. I don't recall any such question as that.

Q. Did the questionnaire received by Ernst & Ernst from the Midwest Stock Exchange make any request that the auditors ascertain whether Rule 27C of the NASD was being complied with by the company?

A. I don't recall any instructions with respect to that.

Q. Did the instructions received by Ernst & Ernst from the Midwest Stock Exchange make any requests that the auditors ascertain whether the company endorsed in writing on an internal record all correspondence pertaining to the solicitation or execution of any securities transaction?

A. I don't recall any questions relating to that.

Q. How mail is handled in a brokerage office is more important to an audit than it is in any other audit, isn't that true?

A. It is more important than in most audits.

Q. Isn't it obvious in the light of your experience in the Nay case that in a brokerage audit, you should ascertain whether or not an officer of a brokerage firm makes a rule that all mail addressed to the firm for his attention should not be opened by anyone but him, so that when he was out of the city, the mail piled up on his desk?

Mr. O'Kane: He didn't testify that he knew of such a rule, so how can he answer such a question?

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: That's right.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. Isn't it obvious that in future audits of brokerage firms, you should inquire whether or not an officer of the company takes regular vacations, and his duties are performed by someone else in his absence?

Mr. O'Kane: May I have the question back about obvious?

(Whereupon the question was read as requested.)

The Witness: A. I think that is an appropriate question to ask.

Mr. King: Q. I hand you a document, which I will ask the reporter to mark Hooker Exhibit 18 for identification.

(Whereupon said exhibit was marked as requested.)

This questionnaire is substantially a copy of SEC Rule 17a-5, is it not?

A. Yes, it is.

Q. The questionnaire used by the New York Stock Exchange for the brokers' audits is almost the same as Hooker Exhibit 18, isn't that true?

A. Yes.

Q. Both questionnaires are copied from SEC Rule 17a-5, are they not?

A. I believe so.

Q. Is it customary to put an SEC facing page on your answers to the Midwest Stock Exchange questionnaire to file with the SEC?

A. Yes.

Q. I notice that the New York Stock Exchange's comparable questionnaire states at the head of the first page: "Answers to be prepared by independent public accountants making the coincident audit." These words do not appear in the Midwest Stock Exchange questionnaire, but their absence is not significant, is it?

Mr. O'Kane: I object to that. That is a legal conclusion which he has to draw. It calls for a state of mind with regard to the authorship of both documents. He can't possibly answer the question.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Yes.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: A. Yes.

Q. The answers to the Midwest Stock Exchange questionnaire are always prepared by the independent public accountant, are they not?

A. I can't say that they are always prepared by the independent public accountant. The independent public accountants are required to express their opinion as to the fair presentation of the answers.

Q. Did you not in audit of the First Securities Company prepare the answers to the first questionnaire?

A. Yes, we did.

Q. And is not this regular standard procedure?

A. With respect to this company?

Q. Or any brokerage audit.

A. I can't answer that for any brokerage audit, but it was for this company.

Q. I notice on the first page of this questionnaire Hooker Exhibit 18, Rule B1 states: "The information pre-

sented shall be sufficient to permit the determination of the financial condition of the respondent." Do you see those words?

A. Yes.

Q. That is why Ernst & Ernst certify on each of these audits that the answers to the financial questionnaire fairly present the financial position of First Securities Company, does it not?

A. Well, instructions require that the questionnaire be accompanied by the report of the independent accountant. I don't know if you can relate it back specifically to just this one instruction here.

Q. Well, must not that report state that the answers to the questionnaire fairly present the financial position of the brokerage company being audited?

A. Only if, in fact, the accountants have come to that conclusion.

Q. Now, will you please look at this Hooker Exhibit 14. I notice from Hooker Exhibit 14 that you answer this nine page printed questionnaire in one sheet with only a few lines. How do you explain that?

A. The instructions state that you are to only answer the questions that are applicable. Read your instruction in A3. If no answer is made to a question or subdivision there, it shall constitute the representation, the respondent has nothing to report. These are the questions that require an answer.

Q. There were sixteen questions to be answered in the questionnaire, and Ernst & Ernst answered only five of those sixteen questions, is not that true?

Mr. O'Kane: Which questionnaire? When you mention sixteen, are you talking about the one in 1970?

Mr. King: The questionnaire, which is Hooker Exhibit 18.

Mr. O'Kane: How can he answer with respect to a document in 1970 when this particular Exhibit No. 14 dates back to October 31, 1967?

Mr. King: Because the document of 1970 is almost

Mr. O'Kane: We don't believe that to be a fact. exactly the same as the prior document.

Mr. Rieger: The witness has already testified.

Mr. O'Kane: No, he has not.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: No. He can answer the question.

Mr. King: Read the question, please.

(Whereupon the question was read as requested.)

Mr. O'Kane: I instruct him not to answer.

Mr. King: You instruct the witness not to answer?

Mr. O'Kane: Yes, sir.

Mr. King: Q. In the questionnaire that you received for Hooker Exhibit 14 for the 1967 audit, the questionnaire was substantially the same as the questionnaire, which is Hooker Exhibit 18, was it not?

The Witness: A. I am not sure if I can say it was substantially the same. The questionnaire was revised in November of 1970. The revised instructions change the number of questions, and instead of being answered in a two column form, it required four columns. Now, whether these changes constitute substantial change, I don't know.

Q. But there were sixteen questions in the questionnaire in 1967, were there not?

A. I believe there were sixteen questions.

Q. Why did you not answer all sixteen questions?

A. The instructions provided that we should answer only the questions that were applicable.

Q. Will you please look at question 14 of Hooker Exhibit 18. I notice that question 14 of this questionnaire

which you did not answer, requires you to state separately contractual commitments that are not recorded in any ledger account for money. That question was asked in the 1967 questionnaire, was it not?

A. Yes.

Q. Why did you not answer that question?

A. If we did not answer the question, it was because there were none.

Q. This question 14 requires you to state commitments of general partners and officers of the company that are substantial in view of the capital of the respondent, does it not?

A. Would you repeat that question, please?

(Whereupon the question was read as requested.)

Yes, it does.

Q. The plaintiffs in this case hold signed commitments by Nay for $975,500. You would require that as substantial in view of the capital of First Securities Company, would you not?

Mr. O'Kane: That has nothing to do with the defendant. Whatever Nay had in his obligation with somebody else and has nothing to do with his knowledge.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Unless the question is asked on behalf of the named defendant.

Mr. King: Q. Do you refuse to answer in accordance with your counsel's instructions?

The Witness: A. Yes.

Q. Question 16 of Hooker Exhibit 18 is captioned: "Unrecorded assets, liabilities and accountabilities, is it not?

A. Yes.

Q. That same question occurred in the questionnaire that you were given in 1967, did it not?

A. I believe so.

Q. It requires you to submit a separate schedule containing a disclosure of any liabilities of the respondent, actual or contingent, which are not included in ledger accounts. Why did you not answer that question?

A. We did not answer the question; it is because there were none.

Q. Question 16 states, and I quote: "Only such items which in the aggregate are material in relation to net capital need be recorded," does it not?

A. Yes.

Q. You would regard items aggregating $975,500 as material in relation to First Securities Company's net capital, would you not?

A. Yes.

Q. I notice under the caption, "Audit requirements" on Page 8 of Hooker Exhibit 18, that the audit, and I quote: "Shall include all procedures necessary under the circumstances to substantiate the assets and liabilities." Do you find that phraseology?

A. Yes.

Q. That was in the questionnaire that you received in 1967, was it not?

A. Yes.

Q. Was it not necessary procedure in the case of your audit of First Securities Company to ascertain whether or not Nay took regular vacations and his duties were performed by some other employees in his absence?

A. Would you repeat that question, please?

(Whereupon the question was read as requested.)

Mr. O'Kane: I object to the form of the question on the basis of "necessary." Necessary for a true accurate portrayal of financial conditions of this company?

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: He can't answer the question when you say "necessary." It is too broad. I am objecting to the form.

Mr. King: Are you instructing him not to answer the question in that form?

Mr. O'Kane: That's right.

Mr. King: Q. Do you refuse to answer in accordance with your counsel's instructions?

The Witness: A. Yes.

Q. Was it not a necessary procedure in your audit of First Securities Company to discover that Nay had a rule that mail addressed to the company for his attention should be opened only by him?

A. Will you read that one back again, please?

(Whereupon the question was read as requested.)

No, it was not a necessary procedure.

Q. I notice on Page 9 of Hooker Exhibit 18 that the auditor is required to obtain a written statement from the officer of the corporation as to the assets, liabilities and the accountabilities contingent or otherwise not recorded on the books of the respondent. That same question was in the questionnaire that was given you in 1967, was it not?

A. I believe so.

Q. I found no such written statement in Hooker Exhibit 14. How do you explain its absence?

A. It would be included in our working papers.

Q. Examination of your working papers by us fail to disclose that. Are you still of the opinion that there was such a written statement?

A. Read that last question back with regard to—the one presented with regard to the written statement by the officer of the corporation.

(Whereupon the question was read as requested.)

We obtained what we call a letter of representations. We get this every year, and I believe it adequately covers this question. I would be surprised if it is not in our working papers.

Q. It is your testimony that you did obtain from Nay the statement required by the questionnaire as to liabilities that are not recorded on the books, is this correct?

A. I believe we have a letter which would cover that.

Q. In general practice, letters to an officer of any business marked "personal" on the outside of the envelope are normally put on his desk without being opened, is not that true?

A. I believe so.

Q. But it is normal office procedure for letters not marked "personal" to be opened by a secretary or someone else in the office, is not that true?

A. I believe so.

Q. Don't you think everyone in the office of First Securities Company knew that mail addressed to the company for Nay's attention piled up on his desk unopened when he was absent for a day or so?

A. Would you repeat that question, please?

(Whereupon the question was read as requested.)

I would assume that at least most of them would see the mail on his desk.

Q. I hand you a document, which has previously been marked Ogren Exhibit 1 in this case. What is this, Mr. Hooker?

A. It is a certificate of membership issued to Leston B. Nay of First Securities Company of Chicago from Midwest Stock Exchange.

Q. You saw this certificate hanging on the wall in the office of First Securities Company, did you not?

A. I don't remember specifically if I did see it. I probably did.

Q. You have no doubt it was there, is not that true?

Mr. O'Kane: That is not what he said.

Mr. King: I will take his answer.

Mr. O'Kane: Thank you.

Mr. King: Q. Don't you think it was unfair of Midwest Stock Exchange without any investigation to have certified Nay in this way and then unloaded on the auditors without any warning of Nay's questionable background the job of discovering his thefts?

Mr. O'Kane: I object to the form of the question.

Mr. Rieger: I object to the form of the question.

Mr. O'Kane: I object to the form of the question.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Right.

Mr. King: Q. Are you refusing to answer in accordance with your counsel's instructions?

The Witness: A. Yes.

Q. The securities business in the United States has a much more complicated accounting problem than most businesses, is not that true?

Mr. O'Kane: I object to that question. It calls for speculation on the part of this witness.

Mr. King: He is offered as an expert CPA. I think he is.

Mr. O'Kane: Ask him then. Lay the proper foundation.

Mr. King: I think I have done so.

Mr. O'Kane: I don't think you have.

Mr. King: Read him the question.

(Whereupon the question was read as requested.)

The Witness: A. I can't say that it is more complicated than most.

Q. It has been necessary at times to shorten the hours of the stock exchanges so that the back offices of the accounting departments can catch up, is not that true?

A. Yes.

Q. The whole business world in the United States relies implicitly upon the certification of brokers' audits by the nationally known accounting firms, is not that true?

Mr. O'Kane: Objection to that particular question.

Mr. King: Are you instructing him not to answer?

Mr. O'Kane: I object to that question as calling for a legal conclusion as to what the state of minds of other people might be and on that basis, I would instruct him not to answer on pure speculation.

Mr. King: Q. Do you refuse to answer in accordance with your counsel's instructions?

The Witness: A. Yes.

Q. The reliance upon audits by the nationally known auditors is necessary to the continuation of the securities business in the United States, is it not?

Mr. O'Kane: I will object to that question. That is a legal conclusion.

Mr. King: Are you instructing the witness not to answer?

Mr. O'Kane: Yes, sir.

Mr. King: Can we have a five minute recess.

(Whereupon a recess was had.)

Mr. King: Q. I am asked to put a hypothetical question to you. Mr. Hooker, if you had discovered in your audits of First Securities Company that Nay as its president took no vacations and had established an office rule that all mail addressed to the company for his attention should not be opened by anyone but him, would you have approved its sytem of internal accounting control?

The Witness: A. Had I known that, I would not have changed our audit program in any way from the program that we followed in those examinations.

Q. Would you have certified had you known that the accounting control system was adequate?

A. We are not required to certify that the accounting control system is adequate.

Q. Would you have reported that your investigation disclosed that the accounting control system was adequate if you had known those facts?

A. We are not required to make that report.

Mr. King: That is all.

Do you have any questions? You don't have any questions, do you, counsel?

Mr. Rieger: No.

Mr. King: What about signature? I think we better do this. We should give the witness a chance to correct the transcript, and so I would like to have it signed, and so I will send it to you.

Mr. Berner: Fine. Counsel, you will attach copies of the documents used.

FURTHER DEPONENT SAITH NOT

IN THE UNITED STATES DISTRICT COURT

* * (Caption—No. 71 C 454) * *

I have read the foregoing transcript of my deposition, consisting of Pages 1 to 71, inclusive, and the foregoing is a true, correct and complete transcript of my deposition so given at the time and place aforesaid, and I subscribe and make oath to the same.

/s/ Jerry M. Hooker
Jerry M. Hooker

Subscribed And Sworn To
before me this 26 day
of October A.D. 1971.
/s/ Norma J. Fillion
Notary Public
My commission Expires Nov. 1, 1974

REPORTER'S CERTIFICATE

State Of Illinois)
) ss:
County Of Cook)

I, Ruth. L. Bernstein, a Notary Public in and for the County of Cook, State of Illinois, do hereby certify that there came before me on the 24th day of August, A.D. 1971, at 10:00 o'clock a.m., at, Suite 4105, 135 South LaSalle Street, Chicago, Illinois, the following-named person: Jerry M. Hooker, who was by me first duly sworn to testify the truth and nothing but the truth of his knowledge touching and concerning the matters in controversy in this cause; that the testimony given by said witness was recorded by me stenographically, and thereafter reduced to typewritten form by me.

I further certify that the foregoing 71 typewritten pages, inclusive, contain a full, true and correct record of the testimony given by said witness, and of all proceedings had upon the taking of his deposition.

I further certify that Messrs. Willard L. King and Stanley N. Gore of the law firm of King, Robin, Gale & Pillinger, appeared on behalf of the Plaintiffs; and that Mr. Mitchell S. Rieger of the law firm of Schiff, Hardin, Waite, Dorschel & Britton, appeared on behalf of Defendant Midwest Stock Exchange; and that Messrs. Harry J. O'Kane and Robert L. Berner, Jr., of the law firm of Baker & McKenzie, appeared on behalf of Defendant Ernst & Ernst.

I further certify that I am neither attorney nor counsel for, nor related to or employed by any of the parties to the action in which this deposition was taken; and further, that I am not a relative or employee of any attorney or counsel employed by the parties hereto, or financially interested in the action.

In Witness Whereof, I have hereunto set my hand and affixed my notarial seal this 23rd day of September, A.D. 1971.

/s/ Ruth L. Bernstein
Ruth L. Bernstein
Notary Public
Cook County, Illinois

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454 and 71 C 1204) * *

The Deposition of Jerry Hooker, taken before Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, at Suite 4105, 135 South La Salle Street, Chicago, Illinois, on Wednesday, April 11, 1973, at 2:30 P.M.

Present:
Mr. Willard King,
Mr. Willard J. Lassers,
Mr. Donald L. Vetter,
appeared for the Plaintiffs;
Messrs. Baker & McKenzie,
By Mr. Robert L. Berner and
Mr. Thomas F. Bridgman,
appeared for the Defendants.

JERRY HOOKER, having been first duly sworn, was examined and testified as follows:

Examination By Mr. Lassers.

Q. For the record, will you state your name, please?
A. Jerry M. Hooker.
Q. And your address?
A. 620 Glendale Drive, Glenview, Illinois.
Q. Glenview what?
A. Illinois 60025.
Q. You are the Jerry M. Hooker who executed an affidavit in this case on December 8, 1972?
A. Yes, I am.
Q. Do you have a copy of your affidavit with you?
A. No.
Q. You are employed by Ernst & Ernst?
A. Yes, I am.
Q. How long have you been with Ernst & Ernst?
A. Since 1957.
Q. You started to work on audits of First Securities Company the very first year you were with Ernst & Ernst, is that correct?
A. Yes.

Q. In what capacity at that time?

A. As an assistant accountant.

Q. How long did you remain an assistant accountant?

A. About two years.

Q. Then what did you become?

A. I've got the dates in here as to that. Assistant accountant two years, senior accountant from 1959 to 1963, a supervisor from 1963 to 1966, a manager from 1966 to 1969, and in 1969 I was admitted to partnership.

Q. In your capacities as a manager from 1966 to 1969, did you have primary responsibility during that period for the audit of First Securities Company books?

A. I had responsibility. I'm not sure I know what you mean by primary.

Q. Did you have a supervisor working under you at that point?

A. Yes, and a senior accountant and an assistant accountant.

Q. A team of how many altogether, four?

A. Counting myself it would be four.

Q. During the period that you were manager when you went out of the office, did you stay there during the entire period of the audit?

A. No.

Q. You had other accounts that you were also manager on, is that right?

A. That's correct.

Q. And you rotated your time among the various accounts?

A. That's right.

Q. Now did the supervisor during this period, was his responsibility then to have his work reviewed by you?

A. Yes.

Q. And you in turn turned over to an Audit Committee for signature by a partner?

A. It went through our review department, the report.

Q. And then after that it went to a partner for signature, is that right?

A. For signature, that's right.

Q. Now you are fully familiar with all of the auditing procedures that were done by Ernst & Ernst during the period from 1957 through the end of the 1967 audit, right?

A. Yes.

Mr. Bridgman: That is in regard to the First Securities account?

Mr. Lassers: Yes.

Q. Are you familiar with the procedures that were used with respect to sending out confirmation requests of First Securities during that period?

The Witness: Yes.

Q. As of the end of the fiscal year?

A. In 1964 the Midwest Stock Exchange required their member firms to be audited on a surprise basis. We selected the date that we performed the audit and did our confirmation work as of that date, which was not the end of the fiscal year.

Q. Then did you make another audit at the end of the fiscal year?

A. We did not.

Q. You made only one audit?

A. Each year.

Q. Each year?

A. That's right.

Q. Did you prepare a financial statement as of the end of the fiscal year?

A. No. At the time we were doing the suprise audits the only thing we did at the end of the year was to prepare the tax return for the company.

Now prior to 1964 we performed our audit as of the end of the fiscal year, which was December 31st.

Q. Did the company maintain a December 31st fiscal year throughout the period that you were working on the audits?

A. For tax purposes?

Q. Yes.

A. Yes.

Mr. Berner: I am sorry, Mr. Lassers, did you say December 1st or 31st?

Mr. Lassers: 31st.

Q. Now how about for purposes of the X17(a) questionnaire to the Securities and Exchange Commission, what fiscal year ending was used for that purpose?

The Witness: December 31st was used prior to 1964. During 1964 and subsequently we used the same date that we used for filing the questionnaire with the Midwest Stock Exchange.

Mr. Lassers: I would like you to mark the answers to financial questionnaires as Hooker Exhibits No. 17 through 26.

(Documents marked as requested.)

Q. Hooker Exhibit No. 17, is that a copy of Part 1 of the Form X17 (a) for 1958 prepared under your auspices?

A. Yes, it's Form X17 (a) 5.

Q. And was that as of the fiscal year and then continuing on through 1963, and I show you Hooker Exhibits No. 18 through 22. Those are the comparable documents for the fiscal year shown, is that correct?

A. Through 1963.

Q. Through 1963, right.

A. Yes.

Q. Then Hooker Exhibit No. 23, which is dated September 30, 1964, that is the comparable document but the September 30, 1964, date reflects the date of the surprise audit for that year, is that correct?

A. That's correct.

Q. After they started the surprise audit procedure, did the date of the surprise audit selected for the report to the SEC and also to the Midwest Stock Exchange—

A. Would you repeat that, please?

Q. You prepared financial statements for the Midwest Stock Exchange as well as for the SEC, right?

A. Right.

Q. And the financial statement to the Midwest Stock Exchange was also as of the date of the surprise audit, right?

A. Yes.

Q. And the same is true for your annual report to the State of Illinois, correct?

A. Correct.

Q. And it was in connection with the surprise audit that you then sent out confirmation statements to the customers, requests for confirmations to the customers, is that right?

A. Right.

Q. In connection with the surprise audit, who selected the date of the surprise audit?

A. We at Ernst & Ernst did.

Q. This was done, and was notice given to the Midwest Stock Exchange?

A. We notified them the quarter that we were going to perform the audit, and then once we started the audit we notified them that the audit had commenced.

Q. Was First Securities told the date of the surprise audit?

A. No.

Q. Did the surprise audit always begin on the last day of a month?

A. No. I think that the earliest it ever began was the second to the last day of the month.

Q. So it was either the second to the last, the next to last, or the last day of the month?

A. Yes, that's right.

Q. What was the first point in time that anybody at First Securities knew when you were coming in on the surprise audit?

A. When we appeared in their offices on the day that we started the audit.

Q. What time in the morning did you appear?

A. Well, as I recall, it varied. At some times we would be there in the morning when they started and at other times we would come there in the afternoon.

Q. When you sent out your confirmation requests, did requests for confirmation go on a selected basis to the customers or were they sent out to every customer?

A. They were sent out to every customer that had a security position or a money balance in their account as of the audit date. In addition to that, we selected some customers with closed accounts and sent confirmation requests to them.

Q. On what basis did you select the closed accounts for sending out confirmation notices?

A. It was a random selection, although we tried to pick some accounts that had some activity during the month.

Q. You mean during the month, you mean during—

A. During the month of the month-end audit.

Q. About how many confirmation requests went out to the closed accounts?

A. I believe about twenty-five.

Q. About how many active accounts did the company have?

A. I believe it ranged between two and three hundred.

Q. Did you receive any complaints with respect to the confirmation notices that you sent out?

A. We received some exceptions which related to in-transit items where securities had been sent in by the customer, say, before the end of the month, and the company received them maybe the first or second day of the following month, or there may have been a check that was in transit at the month-end.

We never received any exceptions that we were not able to resolve to our complete satisfaction.

Q. In connection with your audits did you operate from written instructions?

Q. Who prepared those instructions?

A. They were prepared by various people that had worked on the engagement.

Q. In prior years?

A. In prior years, and then the instructions or the audit program, as we call it, was changed as we felt changes were necessary in the program.

Q. Is the audit program a written document?

A. Yes.

Q. Is that sometimes called the audit calendar?

A. No, no. The audit calendar that we refer to is a calendar of things that must be done on a particu-

lar day, like getting all confirmations out at a particular date, making the account or the securities as of the close of business a certain day. That's what we refer to as a calendar.

We set it up by day and list the various procedures that are to be performed on that day. That usually covers about, for First Securities I recall about five or six days that those specific things were done.

Q. How long did the team remain on the premises to complete the audit?

A. I think generally about two weeks.

Q. You state in your affidavit that you have read the affidavit of Roy Campbell.

A. Yes.

Q. You read that prior to signing your affidavit, is that correct?

A. Yes.

Q. You have?

A. I read that, yes, prior to signing.

Q. Do you recall what is said in the Campbell affidavit with regard to Nay's rules with regard to handling the mail at First Securities?

A. I recall generally.

Q. Would you like to refresh your recollection by rereading the Campbell affidavit?

A. Yes, I recall this.

Q. During the time of the audit at First Securities, did you check the incoming mail as part of the audit?

A. Yes.

Q. How was that procedure handled?

A. We were present at the company's offices in the morning when the mail was brought in and we were looking for securities that were coming in, and we listed those securities and then turned them over to the people in the cage area.

We were also looking for any checks.

We were also looking for any checks. The purpose of this was to try to account for reconciling items that might be in transit as of the audit date.

Q. Were you there at the time that the mail was still tied up in bundles?

A. Are you referring to a particular year?

Q. No, I am speaking now generally during this period.

A. Yes, I recall the mail being tied up in bundles.

Q. Did you watch the opening of the bundles?

A. Yes.

Q. Did you or one of the other auditors actually open the envelopes or was that left to a First Securities employee?

A. As I recall, we were both. We would open the envelopes and they also had knives for splitting the envelopes, but they did it right there in our presence.

Q. If a letter was addressed to Leston B. Nay, was it opened in your presence?

A. I don't believe so.

Q. Were letters addressed to Mr. Nay put aside for him?

A. I believe that all mail addressed to individuals was put aside, and I believe what Mr. Campbell says in his affidavit, that's my recollection, also.

Q. So that the only mail that was opened in your presence were letters that were addressed to simply First Securities Company of Chicago?

A. That's right.

Q. Then the letters were opened. You say that you looked for securities, and if there were any securities in the envelope then you listed them, is that right?

A. That's right.

Q. You listed any incoming checks?

A. That's right.

Q. If there was any correspondence in the letters did you read the correspondence?

A. No.

Q. After you had listed the checks and the securities, did you have anything further to do with the mail?

A. No.

Q. How many days during the course of the audit would you go through this routine?

A. We looked at the outgoing mail starting with the day that we started the audit, and then the incoming mail starting with the first day after the audit date, and did that for two or three days.

Q. So that if an audit, say, began at nine o'clock on Tuesday morning, you did not examine the incoming mail for that Tuesday. Rather, you examined the mail starting Wednesday?

A. If Tuesday was the last day of the month.

Q. Well, regardless of that, but let's just say that you arrived on the premises, "Surprise, here we are," and it is nine o'clock. You did not examine the incoming mail on that day but, rather, on the following day?

A. If the following day was the first day after the audit, that's right.

Q. But you did examine the outgoing mail for the first day, which would be, say, Tuesday?

A. Which would be the last day of the month.

Q. Say it is.

A. Yes.

Q. Did that include everybody's outgoing mail?

A. No, outgoing securities.

Q. Only outgoing securities. So if a salesman wrote to a customer recommending securities, that you didn't concern yourself with?

A. That's right.

Q. Is it correct to say you were only concerned with mail that went out from the cage?

A. Yes, that's right, because all the securities were mailed from the cage.

Q. And also did you concern yourself with checks that went out from the cage?

A. I don't remember if we listed the checks that went out the last day or not.

Q. When was the first time that you became aware of the facts stated in the Campbell affidavit regarding the mail handling practices of First Securities?

Mr. Bridgman: My only objection is I believe he has already answered it. He stated what Mr. Campbell said in his affidavit was aiso his recollection. It is a duplication.

The Witness: I believe that's true. My recollection is, as Mr. Campbell has stated it here. Now when I first became aware of it, I can't say that I became aware of everything that he said my first year on the job, which was 1957.

Mr. Lassers: Q. Let me sharpen up the question to you. Did you ever ask Campbell whether there were any special rules regarding the handling of the mail?

Mr. Bridgman: I object to the characterization of special rules as to whatever that means. I object to the form of the question, also.

If you understand the question as to what special rules.

The Witness: If you mean by special rules that mail addressed to an individual was to be delivered to them unopened, is that what you mean by special rules?

Mr. Lassers: Q. Yes, right.

A. And your question is did I ever question Campbell with regard to those rules?

Q. Yes.

A. I don't recall that I ever did.

Q. Is it correct to say that you learned the substance of what Campbell says in his affidavit about the mail room simply by observing what went on at First Securities?

Mr. Bridgman: I have an objection to the question. If you want to refer to the affidavit, I would expect that it be referred to specifically as to what part of the affidavit. The question is entirely too general for the witness to answer.

Let's get down to specifics in the affidavit, as to what part and place.

Mr. Lassers: I am referring to the Paragraphs 7, 8, and 9.

Mr. Bridgman: I still object. It is entirely too general. I don't know how the witness can answer the question.

Mr. Lassers: Would you like to have the question read? Read the question.

(Record read as requested.)

Mr. Bridgman: Also object to the form of the question.

The Witness: Generally, what Mr. Campbell has said in these paragraphs, No. 7 and 8, I would say yes, I learned of this by observing it to a large extent. Paragraph 9 that you mention there—

Mr. Lassers: Q. That relates to a specific incident.

A. I don't believe I was aware of that instance.

Q. Did you ever speak to Nay himself with regard to rules regarding the handling of mail at First Securities?

A. I don't believe so.

Q. Did you ever speak to any of the mail clerks or any other employee at First Securities?

A. Again, is this with respect to mail addressed to individuals?

Q. No. Did you ever speak to Nay or any employee—

Mr. Bridgman: I believe the witness has already stated he talked to Mr. Campbell.

Mr. Lassers: Q. Okay. Other than Campbell. We are excluding Campbell.

The Witness: Well, I'm sure that I talked with some of the employees about, you know, what time they were going to be down there in the morning to pick up the mail that we wanted to look at. I don't remember specifically.

Q. That is not what I am asking. What I am asking you is whether you ever said to Nay, "Have you given any special rules with regard to handling of mail in this company?"

A. I don't believe I ever asked that question.

Q. Or anything else with regard to the general routine of handling the mail?

A. I don't believe so.

Q. Did you put any such question to any employee at First Securities?

A. I don't believe so.

Q. Did you ever have occasion to discuss questions of internal controls at First Securities with Nay?

Mr. Bridgman: I have an objection as to what is meant by the term internal controls. Unless the term is defined the question is improper in form.

The Witness: Would you like to define what you mean by internal control?

Mr. Lassers: Q. Is internal control a term of art used by auditors?

Mr. Bridgman: Is that a definition, Mr. Lassers?

The Witness: It is a term that's used by auditors.

Mr. Lassers: Q. How would you define it?

A. Accounting internal control?

Q. Yes.

A. It comprises the system used by a company, procedures followed by its employees for reporting, processing, various transactions, a system of internal control that's designed to separate the record keeping functions from the custodian functions to act as a check and balance.

Q. Using the term as you have just defined it, did you ever have occasion to discuss internal accounting controls with Nay?

A. Yes, I believe so.

Q. Do you recall one such topic that you discussed?

A. I believe I was in the discussion as to who should prepare the bank reconciliations.

Q. Approximately when did that discussion take place?

A. I'm afraid I don't remember.

Q. Well, would you put it early in your period, that is, going back to the late fifties, the early sixties, the late sixties?

A. Sometime in the sixties.

Q. Do you recall whether anybody else was present?

A. No, I'm not sure.

Q. Do you recall whether Campbell was present?

Mr. Bridgman: I believe he said he is not sure, Mr. Lassers, who was present.

The Witness: I'm sorry, I'm just not sure.

Mr. Lassers: Q. Do you recall whether any of the other Ernst & Ernst auditors were present?

A. I'm not even sure of the time that I talked with him about it.

Q. Can you relate the substance of the discussion?

A. I believe, and I'm trying to recollect here now, that we had recommended that someone else prepare the bank reconciliations that had no other responsibilities in connection with cash receipts or disbursements.

Q. Was that because somebody who had such responsibilities was doing the reconciling?

A. I think so. I think someone, yes, in the cage.

Q. What did Nay say with regard to that suggestion?

A. Well now, at that time I can't recall, but I know subsequently I'm pretty sure the procedure was changed so that Ms. Ryan, I believe now she's the one, did begin making the bank reconciliations.

Q. Who is Ms. Ryan?

A. His secretary, Mr. Nay's secretary.

Q. She was not a cage person?

A. No, she was not in the cage.

Q. Do you recall whether Ernst & Ernst during this period, 1957-67, ever had occasion to note an exception on your auditor's certificates to the financial statements?

A. An exception to anything, you mean?

Q. Any exception whatever.

A. I believe one year they changed their method of pricing inventories and that we noted the change. Now we refer to that as an exception, anything other than a clean opinion. We were in complete agreement with the change that they had made.

Q. You were in complete agreement?

A. Yes, but it was a matter of consistency. It was not consistent with the preceding year. I can't remember

any other year that we had an exception in our report. We never had an exception dealing with anything other than that.

Q. Did you certify a balance sheet only or did you certify a balance sheet and a profit and loss statement?

A. Through 1963, say from 1957 through 1963 it included, our certification included a profit and loss statement.

In 1964 when we began doing the surprise audits, we did not express our opinion on the income statement.

Q. Was that something that was a change that was agreed upon between you and First Securities?

A. Yes, the reason being—would you like to know the reason?

Q. Yes.

A. The reason being was that since we selected the date ourselves that we would be doing the surprise audit, the P & L period would not be meaningful to them. I mean, it would not be a full year, and so they saw no reason for us to prepare a separate report including a less than a year period to certify to.

Q. Did you know that Nay owned substantially a hundred per cent of First Securities?

A. I know that he owned about ninety-two per cent.

Q. You knew that from 1957, is that correct?

A. There were some minor changes from 1957 on, as I recall, in the capital stock accounts, but I believe that it's safe to say that all during the period he owned at least ninety per cent. I think that's right.

Q. Did the fact that he owned such a high percentage of the capital stock of the company in your opinion pose any special problems with regard to internal controls?

Mr. Bridgman: Internal control as Mr. Hooker has defined it, I assume?

Mr. Lassers: Yes.

The Witness: No, it did not.

Q. Did you ever have a discussion with Nay with regard to the use of pre-numbered receipts for securities?

A. I can't recall discussing that with Nay. I believe that we had written a letter of recommendation back in the forties, I think, where we had recommended they use pre-numbered receipts, but they did not want to use those.

As I recall, they used a Bates numbering machine and numbered each receipt consecutively.

Q. It was—

A. Issued.

Q. —issued. Did you ever have any discussion that you can recall with Nay with regard to this subject?

A. I don't believe so. I don't recall any discussion.

Q. Is it your recollection that during your years there that they were still using receipts which were not pre-numbered?

A. My recollection, yes.

Q. Did you ever have any discussion with Nay with regard to the delivery of securities to customers by salesmen?

A. No, I don't recall any discussions.

Q. Do you ever recall any correspondence with Nay with regard to this point?

A. Delivery of securities to customers by salesmen?

Q. Yes.

A. I don't recall any correspondence.

Q. Do you ever recall becoming aware that such was a practice?

Mr. Bridgman: I certainly object to the form of that question, practice, as to what and by whom, when?

Mr. Lassers: Q. Let me sharpen it up for you. Did it ever come to your attention that salesmen were delivering customers' securities to customers?

The Witness: I don't believe so.

Q. Do you recall whether First Securities had any special form of receipts that were used where a salesman made a delivery of securities to a customer?

A. It's my recollection that all delivery of securities was made from the cage. I don't recall any time a salesman made deliveries.

Q. Does it strengthen internal control if all delivery of securities is made from the cage to customers?

Mr. Bridgman: Again, do we mean by internal control how Mr. Hooker has defined it?

Mr. Lassers: Yes.

The Witness: I believe that's a better system of internal control, to have the deliveries made by the cage rather than the salesmen.

Q. Are you familiar with the rules of the National Association of Securities Dealers?

A. Only somewhat.

Q. You know that there are such rules, is that right?

A. Yes.

Q. In the course of your audits, did you check for compliance with the rules of the National Association of Securities Dealers?

A. No.

Q. More specifically, did you ever check for compliance with NASD Rule 27 (c)?

A. We did not check for compliance with any of their rules.

Q. During the period from 1957 to 1967, are you aware of any changes in the First Securities system of internal controls?

Mr. Bridgman: As that term has been defined by Mr. Hooker?

Mr. Lassers: As defined.

The Witness: The only change I think I recollect is when Ms. Ryan started performing the bank reconciliations that I mentioned previously, and I'm not sure when that was.

Q. When you said that Ms. Ryan performed the bank reconciliations, how did you know that this had occurred? Was it Nay who told you that she was now doing this job?

A. It would have occurred, I believe, in one of two ways. I'm not exactly sure. We have in writing the procedures that are followed at First Securities. We review what we call this write-up of procedures each year.

In connection with this review we would have found out if someone different was performing the bank reconciliations.

In addition to that, First Securities had a very small office, and we would have observed her preparing the bank reconciliations.

Q. If she was reconciling the bank statement while you were there?

A. That's right.

Q. Otherwise, you wouldn't observe it?

A. That's correct.

Q. When did you learn of Nay's suicide?

A. I read about it in the newspaper. I don't know if it was the day it happened or the day before, on the way home that evening I read about it.

Mr. Berner: The day after.

The Witness: The day after.

Mr. Lassers: Q. Are you aware that claims have been allowed in the receivership proceedings by a group of claimants generally referred to as the escrow plaintiffs for approximately $972,000.00?

A. Am I aware that claims have been filed?

Q. Have been allowed.

A. Have been allowed?

Q. Yes.

A. By whom?

Q. By the Court of Appeals, Federal Court of Appeals.

A. No, I'm not aware of that.

Q. Were you aware that claims had been filed by a group of claimants known as the escrow claimants?

A. Yes, I have read the claim.

Q. You have read the claim. But you were not aware that they had been allowed by action of court, is that your testimony?

A. Yes.

Q. Were you aware that a claim has been allowed by the Court of Appeals on behalf of Ms. Elearno Schueren for about $17,000.00?

Mr. Bridgman: I have an objection, Mr. Lassers. In order to avoid confusion, I believe the witness stated that he has read the claim of these people, that is, in this lawsuit, but these claims, in all fairness, I think we should tell the witness are not in this case but are involved in another lawsuit.

Mr. Lassers: All right. That is fair enough. Let me start over again.

Q. Are you aware of a claim of a Ms. Elearno Schueren?

The Witness: A claim that's been filed against us?

Q. No, not against you, a claim filed in—let me go back. Are you aware of a receivership proceedings pending in the United States District Court?

A. Of First Securities?

Q. With a caption, SEC against First Securities Company of Chicago?

A. I wasn't sure of the caption but—

Q. But you are aware of this receivership proceedings, right?

A. Yes.

Q. Now my prior question with regard to the escrow claimants related to a claim filed in that proceedings by the escrow claimants. Were you aware of such a claim?

A. The ones that filed a complaint against us, also, I'm aware of, yes.

Q. Yes, it is the same group, basically the same group.

A. Yes, I'm aware of that group, yes.

Q. Now were you aware of a claim filed by Ms. Eleanor Schueren in the receivership case?

A. I've heard the name mentioned. I'm not sure that I was aware of the claim that was filed. I haven't read anything with respect to Schueren that I recall.

Q. Now we are dealing with claims of Ms. Schueren against First Securities Company, claims as a customer. That is the kind of claim I am speaking of. And your answer is what?

A. I have not read the claim.

Q. But you are aware that such a claim had been filed, right?

A. I think I'm aware that a claim was filed.

Q. Were you aware that the claim had been allowed by the United States Court of Appeals?

A. What does that mean, allowed by the Court of Appeals?

Q. That the Court of Appeals said, in essence, that this is a claim against First Securities Company of Chicago.

A. I wasn't aware of that.

Q. You were not aware of it. But you knew, at least, you knew of the existence of such a claim, right?

A. Yes.

Mr. Bridgman: I believe the witness testified that he thinks he was aware of such a claim.

Mr. Lassers: Q. Were you aware of it at the time you filed the affidavit in this case?

The Witness: I'm not sure when I heard the name Schueren mentioned.

Q. Is it your testimony that you might first have learned of that after you signed this affidavit?

A. See, I'm not even completely sure that I was aware a claim was filed. I have heard the name Schueren. Now whether they filed a claim or not, I'm not sure that I knew that. Can I consult with my attorney here?

Q. You are the witness now. All I'm interested in is finding out what you knew.

A. Okay.

Q. Now before you signed this affidavit, was a draft of this affidavit submitted to you by your counsel?

A. Yes.

Q. That was Mr. Berner?

A. I believe so.

Q. What did you do after you got the draft of that affidavit?

A. I read it and made some changes to it and reviewed it with Mr. Berner.

Q. And then you signed it?

A. Then I signed it.

Q. Did you ask Mr. Berner whether there were any claims that had been filed in the receivership proceedings?

Mr. Bridgman: I have an objection to this. Now we are getting into privileged conversations between counsel and his client. I will instruct the witness not to answer the question.

The content of any such conversations is privileged. We stand on the privilege.

Mr. Lassers: I haven't finished the question yet.

Mr. Bridgman: I thought you did. I am sorry.

Mr. Lassers: Q. That were not reflected on the books of First Securities?

Mr. Bridgman: Same objection as to the content of any conversation between counsel and his client on the basis that the content of those conversations as reflected in the question is privileged from disclosure, and I will instruct the witness not to answer.

Mr. Lassers: Q. Did you make any investigation prior to signing this affidavit whether any claims had been filed and allowed in a receivership proceedings which were not reflected on the books and records of First Securities?

The Witness: Did I make any investigation?

Q. Yes.

A. No, I didn't make any investigation.

Q. Did you make any inquiry of anybody?

Mr. Bridgman: Other than his counsel?

Mr. Lassers: I didn't so limit it.

Q. Did you make any inquiry?

The Witness: I don't remember making any inquiry other than as I said, I read the claim that was filed where we were a defendant.

Q. Against you, Ernst & Ernst?

A. Yes.

Q. Right?

A. That's what I was interested in, yes.

Q. Did you ever read the suicide note that Nay left?

A. I only read about the suicide note in the paper. I have never seen the suicide note.

Q. Did it ever come to your attention in any way that Nay's suicide note said, in substance, that because of his thefts First Securities Company was insolvent?

Mr. Bridgman: Is that the entire content of the note?

The Witness: As I said, I have not seen the note and I'm not sure that I know it said that.

Mr. Lassers: Q. Did it come to your attention in any way that Nay had stated that the company was insolvent?

Mr. Bridgman: I have an objection now. The witness has stated he has never seen or knows of the content of the suicide note.

The Witness: I repeat, I have not seen the suicide note. I don't know what it said.

Mr. Lassers: Q. After the suicide, do you recall whether you made any review of the procedures used to audit First Securities to determine whether there were any weaknesses in the auditing procedure?

A. I reviewed the papers after I read our working papers, after I read about the suicide in the newspaper. I never had any doubt that our audit procedures were adequate, but I did look to see if any of the claims mentioned in the newspapers appeared in our working papers for that last audit, 1967, as a customer.

Q. And what did you find?

A. And I'm almost certain that none of them were.

Q. Now when you say names mentioned in the newspaper, what kind of names?

A. Well, as I recall, they listed two or three or possibly four names of customers or people that were mentioned in the note, saying that he had taken their securities.

Now I had the newspaper article and I checked those names to see if they were customers of the company, and they were not in 1967.

Q. Is this something that you did immediately after you heard of the suicide?

A. The following morning I checked it, yes.

Q. Did you do that on the premises of First Securities?

A. Beg pardon?

Q. Did you do that on the premises of First Securities or at your office?

A. In my office.

Q. At Ernst & Ernst?

A. Yes.

Q. So you did not have access there to the ledger sheets of First Securities?

A. That's right, I did not go to their offices.

Q. Did you have a complete list of the customers of First Securities as part of your audit working papers?

A. Well, I had a complete list of all customers who had a security position or a money balance in their account as of October, 1967.

Q. As of October 31, 1967?

A. Yes.

Q. That was your last audit?

A. Yes.

Q. And your answer is that you found no such customers, right?

A. That's right.

Q. Did you have a list as part of your audit papers of the closed accounts?

A. No, only the closed accounts which we had selected for confirmation.

Q. Did you check those closed accounts?

A. Yes.

Q. Do you recall whether the newspaper accounts that you read announced that these people claimed—

A. I'm not sure. It seems to me that it mentioned one customer with securities over a half a million.

Q. Now linking that customer, does now the name Arnold C. Schuren ring a bell with you?

Mr. Bridgman: In addition to this previous testimony that he has heard the name before?

Mr. Lassers: Right. Can you link up the name Arnold C. Schuren with a claimed loss of half a million?

The Witness: No, it seems like it was listed in the paper as the bank.

Q. Does the name Union Bank of Helena, Montana, ring a bell with you in that connection?

A. I think that was it.

Q. It does.

A. I think that's the name that was in the newspaper.

Q. Do you recall that it said that the Union Bank was the executor of the estate of Arnold Schueren?

A. That I don't remember, who they were the executor of the estate for.

Q. What were the total assets, roughly speaking, of First Securities?

A. As of what date?

Q. As of October 31, 1967.

A. Do I have 1967 here? This goes up through 1964. The total assets are $1,700,895.45.

Q. And the net worth as shown on that balance sheet?

A. It's shown as four numbers, which have to be added and substracted.

Q. Well, but it is—

A. But you can figure it out from this questionnaire, yes.

Q. But it is far, far less than half a million, is it not?

A. Well, let's see. Approximately $130,000.00.

Q. So that if the Union Bank claim was a valid claim, the company would be insolvent, right?

A. If it were a valid claim against the company?

Q. Yes.

A. I believe so.

Q. How much time did you spend on this check that you described a few minutes ago?

Mr. Bridgman: You mean the check that he made of the working papers the day following his knowledge of the suicide?

Mr. Lassers: That is correct.

The Witness: I believe about an hour.

Q. Did you do anything to follow up and do any further checking along those lines?

A. By going through prior years of working papers, you mean?

Q. Yes.

A. Well, I'm not sure if I went back to the preceding year or two or not. I may have done that. We have usually two or three years' working papers in the vault in our office, and the other working papers are stored in a warehouse.

I did not bring in the working papers from the warehouse to go through those, and I'm not sure if I went through two or three years in the office. I remember looking at the last year.

Q. Now did you ever go to any of your superiors at Ernst & Ernst and say to him, "We completed an audit of this company as of October 31, 1967, and now

I have just read in the newspaper that the President of the company committed suicide, and I read that a bank is making a claim for half a million dollars against the company"?

Did you ever relay that fact to your supervisors?

Mr. Bridgman: In those words, I assume?

Mr. Lassers: Not in those words, no, in substance.

The Witness: Well, I'm not sure that the newspaper article said the bank had a claim against the company.

Q. But somebody had a claim, right? That you knew, right?

Mr. Bridgman: Having read it in the newspaper?

Mr. Lassers: Having read it in the newspaper, you knew that somebody was asserting a claim, right?

The Witness: Yes.

Q. Now did you ever discuss that fact with any of your supervisors?

A. Yes.

Q. With whom?

A. I talked with Newell P. Crockett.

Q. Approximately when was that?

A. That day after I read it in the newspaper.

Q. Was this a discussion that you had just as a matter of a piece of news in the newspaper?

A. Well, as a matter of fact, when I was looking through the working papers, he called me and asked me if I had seen it in the newspaper day before, and I told him I had and I was looking through our papers to see if the people mentioned in the newspaper article were listed as customers, and they were not.

Q. Did you relay that information to Mr. Crockett?

A. I was looking through the papers when he called me, and I said, "I'm pretty sure they are not, but I want to go through them one more time to make sure."

Q. After you went through them one more time, then did you call back Crockett?

A. Well, I think I saw him either later in the day or the next day and told him they were not in our working papers as customers of the company.

Q. Did you suggest to him that this was a matter that merited further inquiry?

Mr. Bridgman: What was a matter now, Mr. Lassers?

Mr. Lassers: The fact that somebody was asserting a claim for half a million dollars.

Mr. Bridgman: Against First Securities Company?

Mr. Lassers: Against First Securities that was not reflected on the books of the company.

The Witness: I'm not aware that they were asserting a claim against First Securities Company.

Q. But somebody was asserting a claim, right?

A. Yes.

Q. But did you suggest to Crockett in any way, shape, or form that this was a matter that merited any further investigation?

A. I don't believe so.

Q. Did Crockett make any such suggestion to you?

A. I don't believe so.

Q. Did you have any discussion with any of your other superiors at Ernst & Ernst?

A. Yes.

Q. Who was that?

A. Leroy Kist, who was what we call our technical partner, reviewed the working papers of the last audit to see if in any way he felt our audit procedures had been inadequate.

Upon completion of the review I discussed it with him, and he felt that our audit procedures had been ade-

quate in the circumstances, and that we had done everything required of us to do to express an opinion in the financial questionnaire.

Q. Now when Mr. Kist made that review, did he confine himself to the working papers that you had in your office?

A. I believe so. I believe he looked at all the working papers that were generated in connection with the 1967 audit.

Q. Do you know whether anybody from your organization contacted the Union Bank?

A. I don't know, but I don't believe so.

Q. You didn't?

A. I didn't.

Q. Nobody suggested that you contact the Union Bank?

A. That's correct.

Q. Did anybody else besides Mr. Crockett and Mr. Kist make such review?

Mr. Bridgman: Mr. Crockett did not make a review, Mr. Lassers. He has testified—

Mr. Lassers: Okay. You are right. I stand corrected.

Q. Besides Mr. Kist?

The Witness: I don't believe anyone else did from our office.

Q. From your office?

A. From our office.

Q. And after Mr. Kist made his review and told you what he had found, that was the end of the matter as far as reviews are concerned?

A. Yes, from our office.

Mr. Bridgman: Until you got sued.

The Witness: Yes. Well, then everybody went through our papers.

Mr. Lassers: Do you recall any discussions that you ever had with Nay at First Securities regarding the ending of monthly statements to customers?

A. I can't recall discussing sending monthly statements to customers with Nay.

Q. With Campbell?

A. Yes, I discussed it.

Q. Approximately when did that discussion take place?

A. In 1963, and prior they sent a statement out to customers as of the end of the year, which we included our confirmation request with. In 1964 when we started the surprise audit, they did not prepare statements, but, rather, they used our confirmation forms which were addressed to all the customers that had security positions and/or money balances, and we mailed those out then to the customers.

Q. Do I understand correctly that prior to 1964, as of December 31st, First Securities would prepare a statement showing the customers' security and cash position and you mailed that out requesting confirmation, but after 1963 then did you prepare a statement of position?

A. No, they prepared it on our forms.

Q. As of the end of the month of the surprise audit?

A. Yes.

Q. But did First Securities have a practice of sending out a monthly statement?

A. Can I refer to our write-up of procedures here?

Q. Please. Is this a document that was produced during the prior deposition?

A. Yes.

Q. Let me show you your prior testimony.

A. Our write-up of the procedures states that monthly statements are mailed to customers only at the latter's request.

Q. Would you continue reading that?

A. "We have taken the position in discussions with the client that it was desirable to mail monthly statements to all customers having month-end balances on transactions during the preceding month.

"The client has objected on the grounds that it costs too much. Bad debts are rare and are written off at the time of the annual audit."

Q. Do you recall that discussion?

A. Just vaguely. I think I remember talking with Roy Campbell about this, but I could not give you any indication when.

Q. Do you recall talking to Nay about it?

A. No.

Q. Was it Campbell who stated the cost position in this manner or did he go back and talk to Nay?

A. I'm not sure if he went back and talked to Nay. As I recall, he stated his position on this. It's possible that we mentioned this to Nay, but I just don't recall doing it.

Q. Now the document that you are referring to here is Hooker Exhibit No. 11 from the prior deposition, is that correct?

A. Yes.

Q. Are you familiar with the rules of the Midwest Stock Exchange?

A. With respect to audits of member firms?

Q. Well, generally.

A. Generally.

Q. You know that such rules exist, right?

A. I know that such rules exist.

Q. Are you familiar, is it part of your audit to check for compliance with the Midwest Stock Exchange rules?

A. Yes.

Mr. Lassers: I would like the reporter to mark this report, work sheet headed Capital Requirements, as Hooker Exhibit No. 27.

(Document marked as requested.)

Q. Do you recall preparing such a document as of October 31, 1967?

A. I didn't prepare the document, but I reviewed it.

Q. What was the purpose of this document?

A. To determine if First Securities Company was in compliance with the net capital rules of the Midwest Stock Exchange.

Q. And the document shows that it is not in compliance, is that correct?

A. That's correct.

Q. That there is a deficit of approximately $9,000.00?

A. That's correct.

Q. That was as of October 31, 1967?

A. That's correct.

Q. Did you when you prepared your audit of October 31, 1967, did you note an exception to the financial statements because of that deficit?

A. We did not.

Q. Did you notify the SEC of that deficit?

A. I did not.

Q. To your knowledge did anybody at Ernst & Ernst?

A. To my knowledge, no one did.

Q. Did you or anybody at Ernst & Ernst notify the Midwest Stock Exchange of the deficit?

A. Yes, I did.

Q. Who did you notify there?

A. Mr. Frank Rothing. He was the Vice President.

Q. Was that by telephone?

A. By telephone.

Q. Approximately when did you do that?

A. Between December 1st and December 15, 1967.

Q. Will you relate the substance of that conversation?

A. I called Mr. Rothing and I told him that First Securities did not meet the minimum net capital requirements of the Midwest Stock Exchange by approximately $9.000.00 or $10,000.00. Mr. Rothing was aware of that as of October 31, 1967, that he was further aware that they had corrected the violation, and that they were in compliance now.

I questioned Mr. Rothing if he felt that disclosure of the violation and subsequent correction was desirable in the questionnaire.

He felt that it was not necessary to make such a disclosure. I felt that since it had been corrected, that we did not have to make the disclosure, either.

So I did not make the disclosure in the questionnaire. But I wrote a memo on my telephone conversation with Mr. Rothing, and that's included in my first—

Q. One of the exhibits to your first deposition?

A. Yes, I think it's in there.

Q. Did you discuss this matter with anybody else at Ernst & Ernst?

A. I believe so, because this was, when I wrote this memorandum I had it up as a significant matter and attached it to what we call a review statement that shows the various reviews that have been performed on the work papers and the report, and when it went to the review department I believe I discussed it with the person performing the review department.

Q. Do you remember who that was?

A. I'm not sure at that time. Let's see. 1967. I'm not sure who that person was.

Q. What steps if any did you take to satisfy yourself that in fact the deficiency had been corrected?

A. Well, I would have to refer back to the working papers to answer that. I can't remember now exactly.

Q. Or did you just accept Mr. Rothing's word for it?

Mr. Bridgman: I believe he has already testified he can't recall exactly what he did and I also believe this was covered on the first deposition, in view of Judge McMillan's ruling about duplication of questioning and assessment of costs and expenses.

Mr. Lassers: Q. Do you remember the question?

The Witness: The question was how did we satisfy ourselves that it had been corrected?

Q. Right.

A. And I say I would have to refer back to our working papers to see.

Q. Then I asked you the question whether you just accepted Mr. Rothing's word for it.

A. I don't believe so. I'm fairly certain that we had performed some procedures to be satisfied that the deficiency had been corrected. Exactly what we did though, I don't remember.

Q. You placed your phone call to Mr. Rothing at some time between December 1st and December 15, 1967. It was December 6, 1967. That was the date of your memorandum.

As of December 6th, you would still have been on the premises, is that right, performing the audit?

A. Well, I'm not certain if we had a man over there at that time or not, because I remember making the phone call from my office.

Q. So it might have been after you were already out?

A. But you see, after we finished the audit, the basic

work, then we still get some additional confirmations in that sometimes requires us to go back to the company's office.

As to whether we had a man in there that day or not, I don't recall.

Q. Now referring again to the financial statements for October 31, 1967, do you have that before you?

A. 1967, yes.

Q. I will call your attention to Exhibit No. 26, credit balance of $386,000.00. Was a reserve for bad debts set up with respect to such accounts?

A. Accounts with free credit balances?

Q. Yes.

A. No, sir.

Q. Those were accounts that were owed, that represents money owed to customers, right?

A. Right.

Q. I withdraw the question. Was any reserve for bad debts set up with respect to the collectibility of accounts owed by customers?

A. As of October 31, 1967?

Q. Yes.

A. The answer is no.

Q. With respect to any prior year?

A. I don't recall any reserve for bad debts in prior years.

Q. Now directing your attention here to the item under Question No. 12, amount due from officers, $84,036.72, was any reserve for bad debts set up with respect to that account?

A. No.

Q. Did you know that that was an amount due from Leston Nay?

A. Yes.

Q. Did you make any inquiry as to the collectibility of that item?

A. Yes.

Q. What was the nature of the inquiry that you made?

A. We obtained a confirmation from Mr. Nay that he owed the company this amount, and I believe that we indicated in our working papers when he expected to pay or make payments on the note. I'm not positive of that latter point, but I believe—

Q. You checked with Mr. Nay and you got his statement, yes, he said, "I owe this money." Did you make any investigation as to the collectibility of the debt?

A. Well, not other than the confirmation, the fact that he confirmed he owed it to the company and that he owned approximately ninety-two per cent of the company.

Q. So that your testimony is then that you simply verified that he acknowledged the debt?

A. Yes.

Q. Did you set up any reserve for bad debts with respect to that obligation?

A. No.

Mr. Lassers: I would like the reporter to mark the document headed Internal Control Questionnaire as Exhibit No. 28.

(Document marked as requested.)

Q. Can you identify Exhibit No. 28 for us?

A. Yes, this is our internal control questionnaire which we completed in connection with the audit of First Securities Company of Chicago.

Q. Were you using substantially that same document throughout your years, 1957 to 1967?

A. I believe so.

Q. When you say you completed, you mean that you in the course of your audit investigated each one of the items that are shown on there, is that correct?

A. Yes.

Mr. Lassers: I would like the reporter to mark this group of four exhibits as No. 29.

(Documents marked as requested.)

Q. I ask you if you can identify that group exhibit.

A. These are forms used by First Securities Company.

Q. One of them is a receipt form given to the customer acknowledging receipt of securities, is it not?

A. Yes, one of them is a receipt form.

Q. Substantially that same form was used by First Securities throughout the period that you were on the audit, right?

A. I believe so.

Q. With respect to the accounts receivable due from officers for years prior to 1967, did you follow substantially the same practices that you testified to with regard to 1967?

A. Yes.

Q. That is, you verified the amount obtained from Nay and he acknowledged that he owed the money?

A. Yes.

Q. You did not set up reserves for bad debts in prior years, is that correct?

A. As I recall we did not set up reserves for bad debts.

Mr. Lassers: That is it.

(DEPOSITION CLOSED)

State Of Illinois)
County Of Cook) SS

I, Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, do hereby certify that Jerry Hooker was by me first duly sworn to testify the whole truth, and that the above deposition, recorded stenographically by me, constitutes a true and complete transcript of the testimony given by said deponent;

That the deposition was taken at the time and place indicated above, and that the parties were represented as shown.

In Witness Whereof I have hereunto set my hand and affixed my seal of office at Chicago, Illinois, this 16th day of April, 1973.

/s/ Alberta R. Buster

HOOKER EXHIBIT 1

King's Files

(1)

ERNST & ERNST
CHICAGO

COPY

Hooker Ex 1-P.D.
R.E.

In the Deposition

February 6, 1948

Mr. Leston B. Way, President
First Securities Company of Chicago
134 S. LaSalle Street
Chicago, Illinois

Dear Sir:

In connection with our examination of the accounts of your Company for the year ended December 31, 1947, we reviewed the system of internal control and the accounting procedures, including those relating to the safeguarding of securities. While it is recognized that your system of internal check is necessarily limited to some extent by the relatively small number of accounting and cage personnel, we feel that as many safeguards as may be practicable should be employed. Accordingly, we submit the following comments for your consideration:

We understand that securities held by the Company are counted at regular intervals by the cashiers and comparison with the record of accountability as reflected in the ledger and other records. While the periodic count of securities is considered to be a necessary procedure, in order to be effective the counts should not be made by your cashiers but should be performed by persons other than the custodians of the securities. Also, it is much better to have the counts made at frequent irregular intervals without the prior knowledge of the custodians.

Control over securities due to and from others and held in the box depends, to a large extent, on the ledger and short record. To be effective, this record should be maintained by persons who are not accountable for the securities. However, by the use of prenumbered receipts for all securities received for customers it should be possible to give a considerable measure of assurance that all such securities are actually recorded in the ledger and short records as well as in the customers' accounts. We suggest that you work out a system involving prenumbered security receipts and delivery forms so that this method of control can become an effective part of your accounting procedures.

#2 - Mr. Leston B. Way, President
First Securities Company of Chicago
134 S. LaSalle Street
Chicago, Illinois 2/6/48

We have also been informed that securities are turned over to salesmen for delivery to customers. We urge that this practice be discontinued and that all deliveries be made directly from the cage either by mail or in person. In cases where customers give securities to salesmen for delivery to the Company, it would seem advisable to provide salesmen with a receipt form on which it is indicated that such receipt is temporary and that the customer should expect to receive an official receipt directly from the Company.

In connection with the receipt of cash from customers, your present practice is to use the unnumbered confirmation and statement form when returned by the customer with his remittance or, otherwise, to prepare a three-part unnumbered receipt form, one copy of which is mailed to the customer. We recommend that you consider the introduction of a standard receipt form, which should be prenumbered, for all receipts of cash. In this event, one copy of the form might be used for posting to the customers' ledger instead of, as at present, posting from the cash receipts blotter. The convenience of using tickets for this purpose should tend to offset the additional time required to prepare a form for all cash receipts.

We understand that your bank accounts are periodically reconciled by an officer of the Company. This practice is very desirable and, in our opinion, should be continued.

In general, we would like to point out that the essentials of good internal control involve (1) a separation of the custodianship and recordkeeping functions, (2) independent comparison between securities, cash, and customers' statements, on the one hand, and, on the other hand, the related book records and (3) a system which gives assurance that all transactions are recorded in the accounting records.

A good deal of study by those of your organization who are familiar with the details of your transactions and problems may be required to accomplish the foregoing objectives, but they are of considerable importance and, for this reason, we feel that they should receive the continuing attention of your officers.

BEST COPY AVAILABLE

#3 - Mr. Leaton P. May, President
First Securities Company of Chicago
134 S. LaSalle Street
Chicago, Illinois 2/6/48

During the course of our examination, we reviewed the settlement of balances due from customers at December 31, 1947, and we are pleased to report that there was only one minor violation of the requirements set forth in Regulation T. Our review of your procedures in this respect has indicated a careful administration of the Regulation.

Very truly yours,

Certified Public Accountants

HOOKER EXHIBIT 2

ERNST & ERNST
CONTINENTAL ILLINOIS BANK BLDG.
CHICAGO

Hooker Ex 2 - P.D.
R.B.

ACCOUNTANTS' REPORT

Board of Directors
First Securities Company of Chicago
Chicago, Illinois

We have examined the Answers to Financial Questionnaire of First Securities Company of Chicago as of December 31, 1960. Our examination was made in accordance with generally accepted auditing standards, and accordingly included a review of the system of internal control and the procedures for safeguarding securities and such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying Answers to Financial Questionnaire present fairly the financial position of First Securities Company of Chicago as of December 31, 1960, in the required form and in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Chicago, Illinois
January 13, 1961

HOOKER EXHIBIT 8A

Hooker Ex 8A - R.B.
R.B.

FIRST SECURITIES COMPANY OF CHICAGO

1962 Calendar

Hooker
6

12-31-62 (Mon)

Done 1. Examine bank deposits and accompany to bank
Done 2. Count all securities to lists prepared by client
Done 3. Count petty cash at close of business
Done 4. Count documentary stamps at close of business
Done 5. Examine outgoing mail and accompany to post office ✓
Done 6. Seal security boxes and accompany to vault
Done 7. Request Champaign office to mail in all securities on hand

1-2-63 (Wed)

Done 1. Obtain security boxes from vault, inspect seals and maintain control of boxes until security counts are tied out to proof sheets
Done 2. Mail street confirms (except out of town transfers) after tracing to proof sheets
~~3. Examine bank deposits and accompany to bank~~ delete
Done 4. Examine and list incoming mail ✓
None 5. Mail commitment letters
Done 6. Trace security counts to proof sheets, reconcile differences, if any, and release control over securities

1-3-63 (Thurs)

Done 1. Examine incoming mail ✓
Done 2. Compare, post to proof sheets and mail customers' statements
Done 3. Mail positive confirmations to only 25 closed accounts, stamp balance with negative request stamp
Done 4. Compare long and short records to proof sheets

1-4-63 (Fri)

Done 1. Examine incoming mail and mail transfer confirms to out of town agents ✓

1-7-63 (Mon)

Done 1. Count petty cash at close of business

1-10-63 (Thurs)

Done 1. Mail second request where necessary

(1462)

PREPARED BY [illegible]
APPROVED BY Hooker

Dual Purpose
Voting
Diamond Alkali

Trans

479
1 pp

Transfer agent / Issue	Shares	Name	Certificate
Bankers Trust Company			
Hutchinson Corp - Class A	2	W. H. Schwengel Est	30
"	"	John M. Jackson, Trustee	2218
"	"	Jean Mason	1100
"	"	Dorothy C. Olson	300

264

Aug 9 1962

	INITIALS	DATE
PREPARED BY	Lew Litz	
APPROVED BY	Hooker	

Dist Exam Fee

6

Review of internal control

We reviewed the Company's system of internal control by observation during our examination and by discussions with the Company's employees.

Based on our review we feel that ours and Program adequately reflects the company's procedures as of 6/30/62

HOOKER EXHIBIT 11
(Portions)

Hooker Ex 11 - P 20.
R. B.

CUSTOMERS' ACCOUNTS

Customers' accounts are kept on a bookkeeping machine and are balanced with the general ledger control and with the cage file of P and S tickets (described in subsequent section) monthly by the machine bookkeeper. Postings to the accounts are made from the cash journal, P and S tickets, and receive and deliver tickets (described in subsequent section). Monthly statements are mailed to customers only at the latters' request. We have taken the position in discussions with the client that it was desirable to mail monthly statements to all customers having month-end balances on transactions during the preceding month. The client has objected on the grounds that it costs too much. Bad debts are rare and are written off at the time of the annual audit.

SECURITY INVENTORIES

Security inventories are recorded in the general ledger at market. For year-end tax return purposes, inventories are restated at cost as determined under the first-in, first-out method less a reserve to reduce to the lower of cost or market.

The trade blotters are used as the source for monthly postings to the inventory general ledger control. No detail inventory records are maintained other than the memorandum work sheets of the accounting department and memorandum card record of the trading department. Positions as shown by the memorandum work sheets are marked to the market daily and are used to adjust the general ledger control to market monthly.

S.E.C.
2-6235

OTHER MATTERS

All employees are bonded under a broker's blanket position bond.

Journal entries are prepared by the Cashier and do not require the approval of another officer.

Vacations are taken regularly by all employees and the duties of the employees are assumed by others in their absence.

The Company has not adopted a regular bonus plan, but bonuses are ordinarily paid subject to Company earnings for the year.

EVALUATION OF ACCOUNTING PROCEDURES AND INTERNAL CONTROLS

Based on the foregoing review of the Company's procedures, it is noted that the Company's system of internal control could be strengthened by the incorporation of the following procedures:

1. Monthly mailing of customers' statements.
2. Two officers required to sign checks.
3. By the implementation of prenumbered purchase and sales orders and receipt tickets.

The Company has instituted several procedures that strengthen their system of internal control; these include:

1. Monthly independent reconciliations of bank accounts (other than the payroll account) by the President's secretary.
2. Surprise security counts and reconciliation of the counts to long and short records by representatives of Ernst & Ernst.

3. Surprise annual audits by representatives of Ernst & Ernst, including a 100% circularization of customers' and brokers' accounts.

Due to the fact that receipt and processing of securities, cash receipts and disbursements, and the accessibility to accounting records is centralized in one individual, the Cashier, the overall system of internal control is weak.

AUDIT PROGRAM

FIRST SECURITIES COMPANY OF CHICAGO

We are to examine the Answers to Financial Questionnaire of First Securities Company of Chicago as of the audit date (surprise basis) for the purpose of expressing an opinion thereon. Our examination is to include, but not be limited to, the minimum audit requirements as set forth under Rule X-17A-5 of the Securities and Exchange Commission, and is to be made in accordance with generally accepted auditing standards, and accordingly include a review of the system of internal control and the procedures for safeguarding securities and such tests of the accounting records and such other auditing procedures as we consider necessary in the circumstances.

We are to issue "Answers to Financial Questionnaire" to the Securities and Exchange Commission and the Midwest Stock Exchange (Form X-17A-5) and to the Securities Division, State of Illinois (Form 8B4-2). Our examination will include the audit procedures outlined in the following scopes of examination.

TESTS OF TRANSACTIONS

The purpose of our test of transactions is to provide an evaluation of the Company's accounting procedures and the extent to which they may be relied upon to produce accounting records from which financial statements may be prepared that will present fairly the financial position.

Support of Disbursements

All recorded general disbursements in excess of $50.00, excluding payments to brokers and customers, for the month of April, 1964 will be supported by inspection of invoices and other underlying documents. These disbursements will be traced to the appropriate general ledger accounts. (Payments to brokers and

HOOKER EXHIBIT 16

(16)

FIRST SECURITIES COMPANY OF CHICAGO
135 SOUTH LA SALLE STREET
CHICAGO 3, ILLINOIS

MEMBER
MIDWEST STOCK EXCHANGE

LEBTON B. NAY
PRESIDENT

Hooker Ex. 16 - P. E.
R.B.

TELEPHONE ANDOVER 3-1230
TELETYPE CG-1390

August 22, 1961

Ernst and Ernst
231 South La Salle Street
Chicago 4, Illinois

Attention Mr. Newell P. Crockett

Gentlemen:

Referring to our recent conversations with respect to the strengthening of our internal controls, be advised that beginning with the month of September Mrs. Ryan will reconcile our bank statements monthly.

We also wish to retain you to make three examinations per year of our accountability for securities in safekeeping, etc., on a surprise basis. Since you audit this liability as part of our annual audit, and since our staff does the same incidental to Stock Exchange questionnaires, of which we receive at least two a year as well as on several other occasions, it would appear that this arrangement will be satisfactory to all concerned.

I hope that your estimate of the cost of these examinations by your staff of $100 per will prove to be high.

Very truly yours,

LBN:dr
cc: Mr. Leslie R. Schauffler
for Federal Insurance Company

HOOKER EXHIBITS 17-26

EXHIBIT 17

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 per share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		$ 30,000.00
(c) In treasury (250 shares) — at cost	4,625.00	
(2) Other capital (capital surplus)		16,974.53
(3) Retained earnings (earned surplus)		9,747.53
(d) Reserves:		
To restate house trading securities at the lower of cost or market		60,795.58

QUESTION 12— OTHER ACCOUNTS

• • •

Amounts due from employees	12,652.21	

• • •

EXHIBIT 18

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		$ 30,000.00
(c) In treasury (250 shares) — at cost	4,625.00	
(2) Other capital		16,974.53
(3) Retained earnings		20,836.94
(d) Reserves:		
To restate house trading and investment securities at the lower of cost or market		57,322.06

QUESTION 12— OTHER ACCOUNTS

• • •

Amounts due from employees	12,694.21	

EXHIBIT 19

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		$ 30,000.00
(c) In treasury (250 shares) — at cost	$ 4,625.00	
(2) Other capital		16,974.53
(3) Retained earnings		84,309.82
(d) Reserves:		
To restate house trading and investment securities at the lower of cost or market		8,558.67

QUESTION 12— OTHER ACCOUNTS

• • •

Amounts due from officer	38,850.34

• • •

EXHIBIT 20

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note C:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		$ 30,000.00
(c) In treasury (250 shares) — at cost	$ 4,625.00	
(2) Other capital		16,974.53
(3) Retained earnings		153,381.71
(d) Reserves:		
For trading department losses (commissions withheld)		8,643.24

QUESTION 12— OTHER ACCOUNTS

• • •

Amount due from officer	36,900.00

• • •

EXHIBIT 21

* * *

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		$ 30,000.00
(c) In treasury (895 shares)	$54,931.73	
(2) Other capital		16,974.53
(3) Retained earnings		129,804.31
(d) Reserves:		
For trading department losses (commissions withheld)		9,796.78
To restate house trading and investment securities at the lower of cost or market		6,644.08
To increase securities sold short in house trading accounts to the higher of sales proceeds or market		48.00

QUESTION 12— OTHER ACCOUNTS

* * *

Amount due from officer and employee	40,000.00	

* * *

EXHIBIT 22

* * *

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		$ 30,000.00
(c) In treasury (895 shares)	$54,931.73	
(2) Other capital		16,974.53
(3) Retained earnings		127,001.22
(d) Reserves:		
For trading department losses (commissions withheld)		9,158.52

QUESTION 12— OTHER ACCOUNTS

* * *

Amount due from officer and employee	38,719.00	

* * *

EXHIBIT 23

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		30,000.00
(c) In treasury (895 shares)	54,931.73	
(2) Other capital		16,974.53
(3) Retained earnings (restricted in the amount of $54,931.73, representing the cost of Common Stock in treasury)		121,601.27

QUESTION 12— OTHER ACCOUNTS

• • •

Amounts due from officer and former employee	48,379.70	

• • •

EXHIBIT 24

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		30,000.00
(c) In treasury (895 shares)	54,931.73	
(2) Other capital		16,974.53
(3) Retained earnings (restricted in the amount of $54,931.73, representing the cost of Common Stock in treasury)		117,006.27

QUESTION 12— OTHER ACCOUNTS

• • •

Amounts due from officer and employee	46,900.00

• • •

EXHIBIT 25

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note A:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
(b) Issued (3,000 shares)		30,000.00
(c) In treasury (895 shares)	54,931.73	
(2) Other capital		16,974.53
(3) Retained earnings (restricted in the amount of $54,931.73, representing the cost of Common Stock in treasury)		118,442.27

• • •

EXHIBIT 26

• • •

QUESTION 11 — CAPITAL ACCOUNTS

(c) Corporation capital:		
(1) Capital stock — Note:		
Common Stock, par value $10.00 a share:		
(a) Authorized (5,000 shares — $50,000.00)		
.b) Issued (3,000 shares)		30,000.00
(c) In treasury (895 shares)	54,931.73	
(2) Other capital		16,974.53
(3) Retained earnings (restricted in the amount of $54,931.73, representing the cost of Common Stock in Treasury)		137,922.80

QUESTION 12— OTHER ACCOUNTS

• • •

Amount due from officer	84,436.72

• • •

HOOKER EXHIBIT 27

First Securities Co.
10-31-67
J Page

CAPITAL REQUIREMENTS

MIDWEST STOCK EXCHANGE

NET WORTH

Capital stock: include all classes of common and preferred stock	30,000.00
Less treasury stock	(54,931.73)
Unrealized profit (loss) in firm's investment and trading accounts	
Surplus earned and other capital	154,897.33
Subordinated debentures or other loans to the corporation subordinated to claims of general creditors	
Reserves for valuation and capital reserves	
TOTAL NET WORTH	129,965.60

ILLIQUID ASSETS

Memberships including Exchange Seat	1.00
Furniture and fixtures, less depreciation	1.00
Prepaid and deferred charges	
Leasehold improvements, less amortization	
Miscellaneous receivables	
Unsecured accounts — notes	84,436.72
Other fixed assets	
TOTAL ILLIQUID ASSETS	84,438.72

Hooker, Exh 27
4/11/73

CAPITAL REQUIREMENTS (CONT'D)

RESERVE ON MARKET VALUE OF INVENTORY

Total market value of all municipal and government bonds	
Multiply by 2 1/2% - Reserve requirement on exempt bonds	
Total market value of all corporation bonds rated BBB or above	
Multiply by 12 1/2% - Reserve requirement on top rated corporate bonds	
Total market value of generally liquid corporate securities and corporate bonds not rated BBB or above	
Multiply by 30% - Reserve requirement on general corporate securities	
Total market value of securities in which there is a very limited market and which respondent is principal portion thereof	
Multiply by 50% - Reserve requirement on semiliquid securities	
Total value of securities which have no quoted market - Reserve of 100%	
Total market value of all unsold contractual commitments in when issued and underwriting contracts	
Multiply by appropriate percentage	
TOTAL RESERVE REQUIREMENT	— 0 —

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CAPITAL REQUIREMENTS (CONT'D)

NET CAPITAL BEFORE EXCHANGE REQUIREMENTS

Net worth		120,965.60
Less illiquid assets		<89,439.72>
Less total reserve requirements on inventory		
NET CAPITAL BEFORE EXCHANGE REQUIREMENTS		45,526.88

FIRM'S AGGREGATE INDEBTEDNESS TO GENERAL CREDITORS

All loans to firm that are secured by collateral not owned by firm	
Total of fails to receive on account of customers transactions	425,153.77
Total of items owed to customers	386,720.47
Total of items owed to officers and directors of firm	2,254.28
Total of miscellaneous accounts payable	8,869.00
Total liability reserves	
Money payable against securities in "stock loaned" account	
TOTAL AGGREGATE INDEBTEDNESS	822,997.52

RESERVE REQUIREMENT ON TOTAL OF AGGREGATE INDEBTEDNESS

Up to $375,000.00 of aggregate indebtedness - fixed reserve	$ 25,000.00
Plus 6 2/3% of all aggregate indebtedness above $375,000.00	29,866.51
TOTAL REQUIREMENT ON AGGREGATE INDEBTEDNESS	54,866.51

CAPITAL EXCESS

Net capital before exchange requirement	45,526.88
Less total requirement on aggregate indebtedness	
FIRM'S ~~EXCESS CAPITAL~~	

CLASSIFICATION OF CUSTOMERS' ACCOUNTS

In classifying, consider active securities only.

A - Accounts - Cash Accounts:

1. Long securities and a debit balance
2. Short securities and a credit balance
3. Unsecured debit balances under $100.00 (Banks are exempt from Regulation T)

D - Accounts:

1. Unsecured debit balance over $100.00
2. Short securities without a credit balance

E - Accounts:

1. Credit balance with a contractual commitment (F accounts with an open when issued trade)

F - Accounts - Free Credit Balances:

1. Credit balances with no securities
2. Long securities with no balance - Note A
3. Long securities with a credit balance

X - Accounts:

1. No balance - no securities

Note A - Insert information on confirmation request:

1. Date free (date paid)
2. Location at audit date (from proofsheet)
3. Subsequent disposition - should eventually be delivered or segregated, but we will accept out for transfer n/n

IN THE UNITED STATES DISTRICT COURT

(Caption—Nos. 71 C 454 and 71 C 1204)

The Deposition of Leroy Kist, taken before Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, at Suite 4105, 135 South LaSalle Street, Chicago, Illinois, on Wednesday, April 4, 1973.

Present:
Mr. Willard J. Lassers,
Mr. Willard King,
Mr. Donald L. Vetter,
appeared for the Plaintiffs:
Messrs. Baker & McKenzie
By Mr. Robert L. Berner and
Mr. Thomas F. Bridgman,
appeared for Ernst & Ernst.

LEROY KIST, having been first duly sworn, was examined and testified as follows:

Examination By Mr. Lassers.

Q. Mr. Kist, will you state your name for the record?
A. Leroy E. Kist.
Q. Your address?
A. 848 North Merrill, Park Ridge, Illinois.
Q. Are you the Leroy E. Kist who executed an affidavit in this proceedings?
A. Yes.
Q. On December 8, 1972?
Mr. Bridgman: You want to look at the date?
The Witness: I have a copy of the affidavit.
Mr. Lassers: Q. You are now a partner of Ernst & Ernst?

A. Yes.
Q. How long have you been with Ernst & Ernst?
A. Since 1941.
Q. Are you familiar with First Securities Company of Chicago?
A. Yes.
Q. In what capacity did you begin your work at Ernst & Ernst?
A. I was a junior accountant assisting about 1943 on the First Securities audit, although I'm not so sure that was the name of it then. I think it was called Ryan-Nichols at that time.

I became a senior accountant and then supervisor from a period from 1946 until 1952.

Q. As senior accountant, were you in charge of the audit?
A. I was in charge of the field work.
Q. What is the difference between the functions of the senior accountant and the supervisor?
A. The supervisor ordinarily would have two or three engagements going on at the same time under his general direction, and he would be expected to divide his time on those several engagements so that, in effect, a supervisor would possibly be putting one-third, one-half of his time on the engagement, depending upon its need.
Q. When the supervisor showed up on the scene, did he sit down to work with the others?
A. Ordinarily he would review the progress of the work, review the working papers that had been completed, and determine the continuing scope, see that everything was going along as planned according to the audit program.
Q. But he was not expected, say, to sit down and count securities or whatever else?

A. On the first day of the engagement, ordinarily that's a very busy time. There's a lot of things to do and ordinarily the supervisor would pitch in and work at that time just like anyone else.

Q. So that you say that in the early years, in this 1946 to 1952 period, you were the senior accountant. Did you say later on you were the supervisor?

A. Yes. I don't recall the precise year. I suspect I was advanced to the rank of supervisor in 1948, about 1948. I would be expected to serve as a senior accountant for two or three years.

Q. And then after 1952, did you have any responsibility for First Securities audits?

A. No, I transferred into, I became the Review Department for the Chicago office and I would review the financial statements and form, 17 (a) 5, as it had been completed in the field and brought in for review prior to partner's signature.

Q. You were present here and you heard when we took the deposition of Mr. Crockett?

A. Yes.

Q. You heard his testimony about a Review Committee that reviewed documents after the supervisor finished the work and prior to the signature of a partner. Is that the committee on which you served?

A. That is I. At that time I was it.

Q. You were the only one in the Chicago office, is that it?

A. At that time, I believe, right. It's a full-time job.

Q. In your acting in that capacity you also reviewed the audits of First Securities?

A. The financial statements, the report of the independent auditors, but not the working papers.

Q. So that what was put on your desk then was the X17 (a) 5, for example?

A. Right.

Q. How about the answers to the Midwest Stock Exchange questionnaire?

A. They use the same form as X17(a)5 for the SEC. It just needs a new cover page, possibly a different affidavit.

Q. And I believe the same is true of the report to the Illinois Securities Commission?

A. For a time the Illinois Securities Commission accepted an audited balance sheet and they weren't interested in the X17(a)5 form. Later on they adjusted and changed their rules. I don't know when that change took place.

Q. You also had the audited balance sheet, is that right?

A. Yes.

Q. And you had the document that Mr. Crockett testified to saying in substance, this is okay for signature?

A. It was a review memorandum which the supervisor took responsibility for the completion of the audit in accordance with accepted auditing standards.

Q. That was one page?

A. That was one page. It would frequently be accompanied by notes that had been developed as to matters that had been questioned during the examination and the solutions that were accorded therein.

Q. Now that was it that was presented to you?

A. The audit report in its entirety included a statement of income, notes to the financial statements, balance sheet.

Q. But not the working papers?

A. No.

Q. How about the audit calendar?

A. The audit calendar? That would be part of the working papers.

Q. Was there included any outline of procedures of the steps that were taken?

A. Oh, there's an audit program, on every examination there would be an audit program. I would ascertain that that audit program had been observed from comments made.

The supervisor would indicate that he had followed the audit program, had not deviated from it. That was a pre-determined program.

Q. But those were all with the working papers and you didn't see them?

A. Not unless there was any reason why I felt I wanted to extend my review into the working papers based upon what I could see in the financial statements. I don't recall the necessity of having done that, however.

Q. In the case of First Securities?

A. That's right.

Q. How long did you remain as the Review Committee?

A. Till about 1958. I then went back on the line out in the field and I was admitted to partnership in 1961.

Q. When you went back into the field, did you continue auditing brokerage firms?

A. No, I was mostly on commercial and industrial engagements.

Q. After you became a partner did you work on brokerage firm matters?

A. I keep informed in my present capacity as to the development of matters.

Q. What is your present work as a partner?

A. I'm partner in charge of auditing and accounting for the northwestern district of Ernst & Ernst. I solve

difficult technical problems and review difficult situations and make suggestions for their solution.

Q. Now coming back to your own affidavit and calling attention to Paragraph 4 of Page 2 of your affidavit, the first sentence, which is substantially similar to the equivalent paragraph in Mr. Crockett's affidavit, this refers to a procedure that was done once a year, is that right?

A. Yes.

Q. At that time there were no surprise audits?

A. No.

Mr. Bridgman: At that time again is from 1946 through 1952?

Mr. Lassers: 1946 to 1952.

The Witness: They were not permitted by the Midwest Stock Exchange.

Q. They were not permitted?

A. They were not permitted at that time. The requirement for surprise audit was limited, to my knowledge, to members of the New York Stock Exchange, possibly American Stock Exchange. The New York Stock Exchange members required a surprise audit.

Q. When you say they were not permitted, you mean there was something in the rules that said it should not be a surprise audit?

A. I couldn't be absolutely positive. At least, it was not the practice. It would not be expected that a surprise audit would be followed.

Later on then the Midwest Stock Exchange did change its rules and require surprise audits. I believe they are in the position now of recognizing that surprise audits aren't very good, and they're going to abandon that position, I believe.

Q. So that during 1946 to 1952 there were no surprise audits of First Securities by Ernst & Ernst?

A. Not First Securities Company, no.

Q. And the audits that you referred to, the annual audit, did they commence on the last day of the fiscal year?

A. Either the last day or the day preceding the last day.

Q. And the company knew exactly what day you were coming in, is that correct?

A. Oh, yes.

Q. If you were going to come in on the day before the last day, you told them, "We will come in next Tuesday at nine o'clock"?

A. Yes.

Q. The confirmation notices that were sent out during your time were sent out only to customers that showed a long or a short position or a cash balance?

A. Cash balance, debit or credit, open contractual commitments for unissued securities and closed accounts on a selected basis.

Q. About what percentage of the closed accounts was sent confirmation requests?

A. I would probably tell you a number rather than a percentage. As I recall, the number of open customer accounts at any one time would be about 200, somewhere in that range.

Then we would ordinarily select anywhere from, oh, twenty to fifty closed accounts for negative type confirmation requests, as differentiated from the positive that's used for open accounts.

Q. What do you mean by negative as opposed to positive?

A. Well, a negative request for confirmation sends that statement to the customer with a request that if there's anything wrong, respond. Otherwise, don't bother.

Positive requires a response no matter what, whether it's right or wrong.

Q. How were those closed accounts selected?

A. We would ordinarily select those that had had transactions of any kind within the past three or four months, maybe even six months, and then with a few others selected at random just from the stack of customers' closed account cards.

Q. Coming over to the last sentence of your Paragraph 5 with regard to complaints or comments by customers with respect to escrow investments, do you recall any such complaints or comments by customers with respect to other matters?

A. No.

Mr. Bridgman: By other, other than the escrow?

Mr. Lassers: Other than the escrow, right."

The Witness: Oh, there are always a few items where a customer said, "I mailed you a security, it's not reflected in the records," or, "I sold it," somehow or another, and they were matters which were investigated, follow-up correspondence was made with the customer, and all those discrepancies were always resolved as a routine matter in any audit.

There were no unresolved matters ever left pending at the completion of an audit.

Q. During your period how large was the audit team that went in?

A. The company hadn't changed much. There would be possibly two accountants and a supervisor or a senior, a junior, a supervisor would be the ordinary complement, with a partner in the wings.

Q. Did you operate from written instructions?

A. Yes, an audit program, and a calendar, of course, of timing of doing things.

Q. Was your audit program something developed specifically for this particular audit?

A. Yes.

Q. Who prepared the program?

A. It would be prepared ordinarily by the supervisor and would be approved by the manager or a partner assigned to the engagement.

Q. Was there any standard procedure for these programs laid down by the company?

A. There are minimum audit procedures which are prescribed, that were prescribed then by the SEC that had to be followed.

Our examinations would include those minimum auditing procedures plus other procedures that we felt appropriate.

Q. But there was no firm policy. You couldn't go, say, to a shelf and say broker audit and pull down something Ernst & Ernst had for procedures?

A. Ernst & Ernst procedures, no.

Mr. Bridgman: Like a company handbook or a manual, you mean?

Mr. Lassers: Yes, like a manual, yes.

The Witness: We have an audit manual. Many of the procedures in that manual applied to all types of audits.

A brokerage audit is different only in so far as the securities really are involved, but many types of accounts are the same and the same audit procedures are applied to them.

The special types of procedures are embodied in these minimum audit procedures that are prescribed by the SEC.

Q. When you went in on the first day of your audit, did you make an examination of the mail?

A. Yes.

Q. How many men did you assign to the mail examination?

A. One.

Q. Did you do it yourself?

A. On occasions, yes.

Q. And on other occasions you assigned one of the juniors?

A. When I was a senior I did it. When I was a supervisor I may or may not have done it. I don't recall.

Q. You did it as a senior on the First Securities Company?

A. Yes.

Q. Would you descirbe that procedure for us?

A. Ordinarily, the mail would be picked up by a messenger from the post office. When that messenger, who had no other accounting functions, would bring it back from the post office, we would sit down and possibly an employee of the company and myself would open the mail together and see what was there, and we would list whatever we wanted to list and whatever we wanted to control.

Q. When you first saw the bundle was it still tied up?

A. I don't recall that.

Q. Had it been sorted?

A. No, not to my knowledge.

Q. Were you there to watch the sort?

A. It wasn't that much. Really, you would get a small stack of mail of a dozen or two envelopes. There was no need to sort it particularly.

Q. When you did the job did you open all the letters?

A. As I recall, everything that came in. It used to come in registered mail.

Q. Oh, it was just the registered mail?

A. Registered mail, right. I think that was their usual practice. If there was personal mail, I have no recollection or knowledge of that.

Q. You say this was just the delivery of the registered mail, right?

A. I believe so. We always referred to it as that.

Q. Was it in fact registered mail?

A. Oh, yes. It was customary always to mail securities back and forth registered. Checks could come in, but they would come in with that. I guess the registered mail, we would refer to the registered mail, it would come in with the ordinary mail. It would all come in one big package. There wasn't that much.

Q. You heard Mr. Crockett say that letters that would come in addressed to a salesman would be given to that salesman unopened. Was that your practice, too?

A. I don't recall.

Q. How about letters addressed to Nay?

A. I don't recall ever seeing any. We would only have contact with the mail for possibly three or four days.

Q. Did you do the same steps every day for the three or four days?

A. Yes.

Q. Were you there also for about two or three weeks?

A. As a senior accountant I was.

Q. But as a manager you were there maybe only about a third of the time?

A. Right.

Q. But the engagement still took three weeks?

A. About three weeks.

Q. So when you were there, what about the registered mail, the ordinary mail?

A. Our instructions were that we should inspect all incoming mail during that four-day period.

Q. And that included the registered?

A. Ordinarily securities were always registered.

Q. Was it then the custom, say, if a broker mailed securities to another broker, he always sent it registered, right?

A. Yes.

Q. If a customer sent in securities, it usually came in registered?

A. Yes. The customers, as I recall, were instructed to send their securities registered.

Q. Now did you concentrate your efforts on the registered mail?

A. Only to the extent that that would be securities and we would list all those securities. The other mail, we would look at it, open it, see if it contained checks, and make a listing of those checks, see what they were.

They would help us to resolve any differences that might be reported to us later on by customers.

If he said, "This balance is all paid for," and if we saw on January 2nd a check dated December 30th we were reasonably assured that that was so.

Q. Did you read the mail that came in?

A. No.

Q. Did you open the non-registered mail?

A. Yes.

Q. You were looking for checks?

A. I didn't open it. The company employee opened it. I was sitting alongside of him. That would be my procedure.

Q. If there was an envelope that was opened and there was no check and no security inside, did you have anything further to do with that letter?

A. I don't recall anything like that. What would be in it if it wasn't money or securities? That was their business.

Q. Well, what about if a customer wrote in and said, "I haven't received my stock. Why haven't you sent me my credit balance"?

A. I never saw anything like that of any kind. We would make out the customer's statement and request confirmation of those, at that time we would get the correspondence direct.

Q. That you would read?

A. Every bit of it. We maintained control and duplicate copies.

Q. But of the non-registered mail, if a letter came in and it was not, it didn't have a check and it didn't have any securities in it, did you read the letter?

A. I don't recall ever seeing any letter like that, so I can't answer that one.

Q. After you listed the securities did you also list the checks?

A. Yes.

Q. Then did you give all the mail back to the mail clerk?

A. I don't recall now. We had control of it at that time so I don't think we had any more interest in it. We knew what it was. We knew we had control over it. We were maintaining control over the security boxes, so that the mail then lost its interest for us.

Q. You just gave it back to the mail clerk?

A. Well, whoever was the proper person who entered it in the accounting records. They would ordinarily issue receipts if it were securities received or a check received, there would be a receipt issued.

Q. During your period did you audit just the balance sheet?

A. No.

Q. Did you certify the profit and loss statement as well?

A. Yes.

Q. Was that required by any regulation or was that something that you were hired to do by First Securities?

A. We were engaged to audit the financial statements, all the financial statements of the company. We were not limited at that time, and I don't know whether they ever were. We gave an opinion on the complete financial statement.

Q. Do you recall whether the scope of the certification was ever enlarged or reduced?

A. You mean was a qualified opinion ever expressed?

Q. Yes.

A. Never, to my knowledge.

Q. Was any exception ever taken in any of the certificates to the financial statement?

A. None that I recall.

Q. Have you read the affidavit of Campbell?

A. No.

Q. That I previously referred to?

A. No.

Q. I would like you to read it at this time.

I believe you said that you did not read the Campbell affidavit prior to this moment.

A. No, I did not.

Q. Were you aware of any of the procedures that Campbell describes regarding handling of mail at First Securities?

Mr. Bridgman: Again, this is from 1946 to 1952?

Mr. Lassers: Yes.

The Witness: I don't recall, remember the names of the persons he referred to. I do remember that there was a girl, a woman who did participate in controlling the mail, opening the mail at the time. That would be the person that either myself or my accountant under me would be alongside as she started to open the mail.

Q. Were you aware of the fact that all mail bearing the name of an individual was put on his desk unopened?

A. No.

Q. Were you aware of the fact that Nay's mail was put on his desk unopened?

A. No.

Q. Did you ever ask anybody at First Securities with regard to the practices with regard to handling the mail?

A. Yes.

Q. Who did you put those questions to?

A. Well, I think we would ask probably Roy Campbell what were the procedures, and then he would say, "Well, it's our procedure that the mail would be opened by this woman."

And I would ask her then, "Do you do that regularly?"

We were particularly interested in the checks when they came in, were they controlled right then. And we suggested at one time that they should be taped and a tape retained by her for later comparison with the actual cash receipts journal.

Q. Do you recall about when that suggestion was made?

A. Sometime in the 1940's.

Q. Did you make that suggestion to the mail clerk or did you make that suggestion to Campbell?

A. Ordinarily our suggestions would be developed during the course of the audit as a consequence of our review of the system of internal control, and we would write a letter addressed to the Board of Directors of the company at the conclusion of our audit, and we would have contained in that letter recommendations for strengthening the system of internal control.

Q. You believe that such a suggestion would be included in one such letter?

A. I suspect that back that time we recommended that the mail be controlled.

Q. After you made the suggestion, during the year between the time that letter goes out and the next audit, did you make any inquiries to see whether that suggestion had been accepted and implemented?

A. I don't recall precisely, although it would be our practice to offer to discuss the contents of our letter of recommendations with Mr. Nay and help any questions about that or if he found something about that, why, we would discuss, if he asked me, "Why do you think that is important," we would explain that.

Q. With regard to that specific suggestion regarding making a tape and saving the tape, do you recall suggesting that you talk this over with Nay?

A. I don't recall.

Q. Were all your negotiations and discussions with Nay?

A. Either Nay or Campbell, depending upon the nature of the question or how it could be implemented. We were interested in improving the accounting records.

Q. When you got there for the following year's audit, did you make any inquiry to see whether previous suggestions had been put into practice?

A. Yes.

Q. Do you recall whether that particular suggestion was put into practice?

A. I believe so, yes, because it was being done.

Q. Did you say that you did not know that mail addressed to a specific person was customarily put on that person's desk unopened?

A. I would assume we would accept the fact that mail that was marked personal would be put on a person's desk unopened.

Q. Now I am not talking now about envelopes that were marked personal. My question is, did you know at the time that if a letter came in addressed, Mr. XY, First Securities Company, that under their procedures that letter would be put on XY's desk unopend?

A. No.

Q. Did you know at the time that a similar procedure was being followed with respect to Nay's mail?

A. No.

Q. You say that you inquired of the mail clerk about the procedures and, I take it you asked the mail clerk if she made a tape of incoming checks.

Do you recall anything else that you asked the mail clerk about the procedures?

A. I don't recall any specific questions, generally just the control over the mail. We were interested in seeing that a record was made of incoming mail before it was given to anyone that would have also control over the record keeping, other record keeping or the securities, for example. We wanted the dual control aspects of it.

Q. Apart from this matter about the making of the tape and so on, do you recall any other recommendations that you made to First Securities with regard to internal controls?

A. I don't recall definitely whether they always used prenumbered receipt forms. I seem to recall that they did not, and we did recommend that they institute that procedure.

That was done early in the 1940's. They had a very good accounting system.

Q. Was that suggestion regarding prenumbered receipts, did that relate to receipts for securities received from customers?

A. And cash.

Q. And cash. Did you discuss that with Nay?

A. All matters were discussed with him. We wrote him a letter making those recommendations to him.

Q. And then was the discussion followed up with a conference?

A. Ordinarily? Yes. We frequently had what we would refer to as a closing conference; upon the conclusion of any examination we would relate to him what our suggestions were for improving their accounting records, and then later on we would follow it up with a written communication.

Q. Was this before or after the final typing of the certified statements?

A. The letter of recommendations?

Q. No, the conference.

A. Oh, the conference would be before the final typing, the final report. It would be a preliminary basis.

These are the financial statements of the company and we say these are the financial statements, these are your financial statements, and we think they're all right, or we think there should be some changes made, or what-not, and then those recommendations would be acted upon.

Q. They were in longhand and you passed them around?

A. Sometimes they were and sometimes they were typed up preliminarily.

Q. What was Nay's response to your suggestion regarding the use of prenumbered receipts?

A. He was always extremely cooperative.

Q. Was this something that was in fact implemented?

A. Pardon me?

Q. Was this in fact something implemented?

Mr. Bridgman: This, you mean the adoption of the use of numbered receipts?

Mr. Lassers: Yes.

The Witness: It was, yes.

Q. Did you know that Nay owned practically 100 per cent?

A. Yes, not always.

Q. Of First Securities?

A. Not when I first started there.

Q. What percentage did he own at the beginning?

A. I didn't even know. He was only a Vice President when I started with him.

Q. He had no ownership when you first started?

A. I don't recall. At that point when I was a junior accountant I didn't get into the reading of the minutes or the stock records. I just didn't know.

Q. But in later years he had acquired substantially 100 per cent ownership?

A. Yes.

Q. In your opinion did the fact that he had nearly 100 per cent ownership of the company have any bearing on problems of internal control?

A. No.

Q. Did you ever have any discussion with Nay with regard to the practice of turning securities over to salesmen for delivery to customers?

A. No.

Q. Ever any such discussion with Campbell?

A. No.

Q. Anybody else?

A. Other than we would frown upon that practice.

Q. Do you recall observing or finding out that it existed?

A. I don't specifically recall, although I do know that we would have said that this is not a good practice, it should not be done.

Q. Do you ever recall any discussions with Nay with regard to a suggestion that if a salesman delivers securities to a customer and got a receipt, the receipt should be marked "Temporary Receipt"?

A. I recall something like that. Then a final receipt was sent to the customer by mail.

Q. And that the temporary receipt should bear a notation, "This is a temporary receipt"?

A. Yes.

Q. Do you recall whether that suggestion was ever implemented?

A. Vaguely, yes.

Q. To your knowledge did Nay have access to the cage?

A. He owned the company. He could go any place he liked. But he did not go in the cage, to my knowledge, although he could have had access. He could have changed the rules any time he wanted to since he owned the company.

Q. There are no Midwest Stock Exchange rules that say only so and so can get into the cage?

A. That's right, no such rules that I am aware of.

Q. Of any public body or any supervising authority that you know of?

A. No.

Q. I take it you are aware of the fact that there is a National Association of Securities Dealers.

A. Yes.

Q. Are you familiar with their rules or regulations?

A. I know they exist. I'm not familiar with them.

Q. When you were making your audits did you ever check for compliance with their rules and regulations?

Mr. Bridgman: Object to the question as it presupposes an obligation to do and there is no proper foundation. Go ahead, you can answer.

The Witness: We had the NASD service, the loose-leaf service in our library, and at some time, I worked on many, many audits for security dealers, I skimmed through them to see if there was anything that would apply to our audit, and I discovered none.

Mr. Lassers: Q. Particularly you did not check for compliance with NASD Rule 27(c) relating to listing of incoming and outgoing correspondence relating to customers?

Mr. Bridgman: Same objection, in view of the witness's last answer that nothing applied to the audit.

The Witness: No.

Mr. Lassers: Q. During the period that you were responsible for the audits, were there any substantial changes in First Securities accounting practices?

A. No.

Q. Systems of internal controls?

A. Substantial no. As I mentioned before, we made recommendations from time to time. There was nothing that would be deemed truly substantial.

There were improvements. There was a constant need to improve always on everything.

Q. Did you ever report to the SEC any weaknesses in the internal controls of First Securities?

A. No.

Q. To the NASD?

A. No.

Q. To the Midwest Stock Exchange?

A. No.

Q. Your supervisor?

A. No, other than in the preparation of this letter of comments. They were not of such scope that they would interfere with our giving our opinion, and we would ordinarily, if there were a weakness discovered, we would extend our audit procedures to compensate for that.

Q. When did you learn of Nay's suicide?

A. Pardon?

Q. When did you learn of Nay's suicide?

A. I guess the following morning in the paper.

Q. Are you aware of the receivership proceedings that are pending in the District Court under No. 68 C 1053?

A. Only when you talked to Mr. Crockett about it.

Q. You were only aware of Ernst & Ernst, is that correct?

A. Yes.

Q. Were you aware generally that there was a legal proceedings pending apart from this case?

A. No.

Q. Were you aware of the fact that a claim had been allowed in a receivership proceedings on behalf of Ms. Nora Moyer?

A. No.

Q. With respect to a liability of the company that was not reflected on its books?

A. No.

Q. How about a claim for Ms. Eleanor Schueren?

A. No.

Q. A claim for the Union Bank & Trust Company of Helena, Montana?

A. No.

Q. Were you aware at any time that there had been claims allowed other than the escrow claims for liabilities of First Securities?

A. No.

Q. Claims by customers?

A. No.

Q. Did you participate in any conferences at Ernst & Ernst after Nay's death with respect to the adequacy or completeness of Ernst & Ernst's auditing practices?

A. No.

Q. Were you aware of any such conferences?

A. No.

Q. Are you aware of any changes that were made of Ernst & Ernst brokerage auditing practices as a result of the First Securities matter?

A. There were none.

Q. There were none?

A. There were none.

Q. Was your affidavit prepared in the first instance by Mr. Berner?

A. I don't know. Actually, I didn't think I was going to be involved in this case, since it's been twenty-one years since I was directly associated with the client, and I believe that this was developed with Mr. Berner and I received a draft copy of it and I made some suggestions for revision of it, and that's it.

Q. What you received then was a draft that had been prepared by your counsel, is that right?

A. I believe so.

Q. Do you recall who the Directors of the company were during the period that you were responsible?

A. I remember some of them.

Q. I take it Mr. Nay was a Director?

A. Mr. Nay was a Director.

Q. Anybody else?

A. He was a Vice President in the early forties. A fellow by the name of Walker.

Q. Do you recall his first name?

A. No, I don't.

Q. Was he an employee of the company?

A. He was Vice President.

Q. Anybody else you recall?

A. Mr. Stevens was a bond trader and Vice President. I seem to recall Owen VanCamp. At one time they merged. I'm not so sure what I know during the period of time, though.

Q. He was also an officer and employee?

A. Correct.

Q. Was there any Director that you know of who was not an officer or employee?

A. No.

Examination By Mr. Berner.

Q. I have a question I would like to ask Mr. Kist, if I may. Mr. Kist, you earlier referred to the use of a tape by the mail clerk to record checks received in the mail.

A. Yes.

Q. Is it correct that this would be a control to determine whether the cashier properly recorded the cash received?

A. Yes.

Q. This would not be a control over the person who received the mail?

A. No.

Mr. Berner: I have no other questions.

(DEPOSITION CLOSED)

State Of Illinois)
County Of Cook) SS

I, Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, do hereby certify that Leroy Kist was by me first duly sworn to testify the whole truth, and that the above deposition, recorded stenographically by me, constitutes a true and complete transcript of the testimony given by said deponent;

That the deposition was taken at the time and place indicated above, and that the parties were represented by counsel as shown.

In Witness Whereof I have hereunto set my hand and affixed my seal of office at Chicago, Illinois, this 10th day of April, 1973.

/s/ Alberta R. Buster

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454 and 71 C 1204) * *

The Deposition of Newell Crockett, taken before Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, at Suite 4105, 135 South LaSalle Street, Chicago, Illinois, on Wednesday, April 4, 1973, at 2:30 P. M.

Present:

Mr. Willard King,
Mr. Willard J. Lassers,
Mr. Donald L. Vetter,
appeared for the Plaintiffs;

Messrs. Baker & McKenzie,
By Mr. Robert L. Berner and
Mr. Thomas F. Bridgman,
appeared for Ernst & Ernst.

Mr. Lassers: Let the record show that this is the deposition of Newell P. Crockett, taken at 2:30 on April 4, 1973, pursuant to notice to the parties.

Mr. Bridgman, could we have a stipulation waiving the signature?

Mr. Bridgman: Why don't we wait till the end of the deposition, okay?

Mr. Lassers: All right.

Mr. King: I don't want to waive signature. I want him to sign it.

Mr. Bridgman: That solves the problem.

NEWELL CROCKETT, having been first duly sworn, was examined and testified as follows:

Examination By Mr. Lassers.

Q. For the record, Mr. Crockett, will you state your name?

A. Newell P. Crockett.

Q. Your address?

A. Office, home?

Q. Home.

A. 380 Sterling Road, Kenilworth.

Q. Illinois?

A. Illinois.

Q. You are the Newell P. Crockett who executed an affidavit in this case on December 11, 1972?

A. Yes.

Q. By whom are you employed?

A. I'm a partner in Ernst & Ernst.

Q. And that is the defendant in this case, one of the defendants in this case?

A. Yes.

Q. You are familiar with the First Securities Company of Chicago?

A. I'm familiar with the First Securities Company, yes.

Q. Did you participate in the audits of First Securities Company of Chicago?

A. I did.

Q. During what period of time were you active in auditing First Securities?

A. 1952 to 1957, as I recall.

Q. When you began your work in 1952, in what capacity did you act as auditor?

A. I was the supervising accountant on the engagement.

Q. How many accountants did you have working under you?

A. Probably two.

Q. Did the number vary during this period?

A. No, I believe that there was usually always two.

Q. During the entire period from 1952 to 1961, did you remain in the same capacity in performing the audits?

A. Till 1957.

Q. I am sorry, to 1957. It was 1952 to 1957?

A. Right. In 1956 I assumed a manager's position on our staff, and I had more of a supervisor role than I had formerly, but I still was directly concerned with First Securities.

Q. You say you became a manager in 1957?

A. 1956, end of 1956.

Q. That meant that when you did the audit for 1956 you did it in your capacity as manager, is that right?

A. Yes.

Q. In your capacity as manager did you also go out physically to the offices of First Securities?

A. Yes.

Q. As you had in the past?

A. Yes.

Q. I take it the period from 1952 on you actually went with your two subordinates and performed the auditing work on the premises of First Securities?

A. Yes.

Q. It was then located at 134 South LaSalle Street, Chicago?

A. Yes.

Q. Was there any difference in the nature or character of the services that you performed on the audit at First Securities after you became a manager in 1956?

A. Well, I suppose, and I have to make a sort of a supposition here, I would assume that I wasn't there every day in 1956, that some of the work was done by other people more extensively than it had been done prior to that time.

Q. Was somebody else appointed supervisor on the audit?

A. I honestly don't remember.

Q. Was it company practice at that time that after you became a manager that somebody else would have been appointed as supervisor?

A. On an assignment—I doubt if another supervisor was assigned at that time.

Q. But in any event, was a third man assigned then in 1956?

A. I don't believe so.

Q. Did you also do the audit for 1957?

A. I don't think so.

Q. That would have been—

A. The end of it, yes. My recollection is that 1956 was the last time.

Q. Then after 1957 did you have any direct role in the auditing of First Securities?

A. Not direct.

Q. You had some then in an indirect capacity?

A. Yes. I was still, you know, the manager that had responsibility for the work that was done at First Securities. I was not on the premises except in very rare instances.

Q. I don't understand the difference in your role as manager and your role as supervisor.

A. I'm more directly involved in the work that's being done in the client's office.

Q. Well, then after 1957 did you still have some responsibility?

A. Some responsibility.

Q. Were the audits submitted to your for review?

A. Yes.

Q. How long did that condition continue?

A. Well, a number of years, probably seven or eight or ten, perhaps.

Q. That would carry it up as late as 1967?

A. I don't remember. I don't believe I continued to the end. I don't believe so. I think Mr. Hooker had taken over my role perhaps in the early or mid-sixties.

Q. And thereafter you had no further responsibilities regarding First Securities, is that correct?

A. That's correct.

Q. Now directing your attention to Paragraph 4 on Page 2 of your affidavit—do you have a copy?

A. Yes, I do.

Q. Directing your attention to the first sentence of Paragraph 4 where you say, "All customers of First Securities whose accounts reflected long or short securities positions, cash positions other than zero, or open contractual commitments as of the annual audit date received a request from First Securities initiated by Ernst & Ernst for a written confirmation to be made directly to Ernst & Ernst as to the accuracy of the statements of their accounts with First Securities."

How often were these confirmations sent out?

A. Once a year.

Q. And that was in connection with the annual audit?

A. Yes.

Q. This is an annual audit that was done as of the close of the fiscal year of First Securities?

A. Yes.

Q. Is this a date that would be known to First Securities in advance?

A. Yes.

Q. They selected the close of the fiscal year?

A. Yes.

Q. And, consequently, this would be a date that would be known to Leston B. Nay?

A. Yes.

Q. Did you know Nay?

A. Yes.

Q. You knew that he was President of First Securities?

A. Yes.

Q. Did you know Frank Campbell?

A. Roy.

Q. Roy Campbell?

A. Yes.

Q. In connection with the sentence that I just read you, was a confirmation request sent to an account which showed a zero balance?

A. We tested a few.

Q. What do you mean by a few?

A. We selected some and sent a limited number to those with zero balances.

Q. Who made the selection?

A. Me or somebody else at random.

Q. When you say at random, do you mean that you went though and you said, "We will mail them to every twentieth account"?

A. I can't remember our selection process at First Securities. It might not have been every twenty. I don't know. I doubt if it was. But it would be some number on that basis.

Q. Was it done on a random basis?

A. Yes.

Q. However the random number was selected, it was done on a random basis, is that right?

A. Yes.

Q. About what percentage of the accounts did you aim to send out confirmations?

Mr. Bridgman: Excuse me. Those accounts of zero balance?

Mr. Lassers: Yes.

The Witness: Very small percentage.

Q. One per cent?

A. One per cent, perhaps less.

Q. Coming over now to Paragraph 4, the last sentence in the paragraph, I will read it to you:

"No customers at any time ever informed Ernst & Ernst that their securities position account balances or

statements of open contractual commitments were incorrect because they did not reflect transactions or positions with respect to the alleged escrow or that any amount of escrow investments were owed to them by First Securities."

Were there any customers who made complaints to Ernst & Ernst in response to these confirmation requests, who complained that their accounts were inaccurate in other respects other than the escrow?

A. I would assume so.

Q. Do you recall specifically?

A. I don't think there's any brokerage engagement that wouldn't have complaints about transactions not having been recorded, such as the shipment, a customer sent securities at the end of the year and they're not recorded on his account, or a trade was executed and it wasn't recorded on his account because there's a period of time there when things are not recorded.

Q. Did any particular item stand out in your mind at that point?

A. No.

Q. In your role as manager and supervisor, did you assign the work to the two other members of the team?

A. Yes.

Q. And they worked under your direction and control?

Mr. King: The reporter doesn't get your nod, so you have to utter.

The Witness: Yes.

Mr. Lassers: Q. Was checking the mail a part of the procedure for your audit?

A. It was.

Q. About how long did you spend on the annual audit?

A. Three weeks.

Q. Did that mean that the three-man team worked full-time for three weeks?

A. Two or three.

Q. And of that, how much time was spent on the premises of First Securities.

A. Most of that, almost all of it.

Q. So that if you would get there in the morning you would be there working full-time on the premises for about three weeks?

A. Yes.

Q. And then how much time did you have to complete the work when you got back to the Ernst & Ernst office?

A. I don't recall exactly, but I think our reports had to be out by February 15th or thereabouts.

Q. This is for fiscal year that ended when?

A. December 31st.

Q. My question is this: You say that the whole work took you three weeks, and of that, how much of that three weeks was spent on the premises of First Securities?

A. I'm talking about the time spent on the premises essentially. It was somewhere between two and three weeks.

Q. Then how much time was spent back at the Ernst & Ernst offices completing the work?

A. Are you talking about manhours now?

Q. Yes, manhours.

A. Probably one more week.

Q. All three of you would have another weeks' work?

A. No, one more manhour week.

Q. Now will you describe for me the nature of the check that you made with respect to the First Securities mail?

A. We checked incoming securities for, I believe the day the audit started, which was December 31st, but I'm not positive of that, and one or two days thereafter.

Q. Was the mail check carried out by all three members of the team?

A. No, usually one.

Q. Did you participate yourself personally?

A. I don't think so.

Q. Was this a job that you delegated then to your subordinates?

A. Yes.

Q. Do you recall whether you delegated one man or did you delegate both of your men?

A. I would have to guess it would be one.

Q. At any rate, you were there with him on the premises?

A. Yes.

Q. Was this first day a day that was known in advance to First Securities?

A. Yes.

Q. There was no surprise about this?

A. No.

Q. So when you went down there in the morning, did you pick up the mail at the post office?

A. No, in the offices of First Securities.

Q. And what time did you get there?

A. Quarter to nine, I presume, 8:30, quarter to nine.

Q. Were the offices open at the time you arrived?

A. Yes.

Q. Do you recall what time they started business?

A. No, but I'm sure approximately that, 8:30 or quarter to nine.

Q. Was the mail already, the twine already off the mail?

A. I have no idea.

Q. Was it part of your routine to try to get there before the twine was off the mail?

A. No.

Q. You didn't care about that?

A. No.

Q. Had the mail been sorted before you looked at it?

A. Yes.

Q. And sorted in what sense?

A. Mail addressed to First Securities Company of Chicago was supposed to be turned over to us unopened.

Q. But all the mail that came in there was all First Securities mail?

A. I don't know.

Q. Let's say that if a letter came in addressed to a salesman, was that supposed to be turned over to you?

A. No.

Q. What about a letter addressed to Nay?

A. No.

Q. What about a letter addressed to Nay, President, First Securities?

A. No.

Q. A letter, First Securities, attention Leston B. Nay?

A. No.

Q. The only mail that you examined was the mail that said just First Securities Company of Chicago?

A. We were looking for securities being transmitted to First Securities Company.

Q. Then you or your subordinate opened the mail?

A. Yes.

Q. If there were any securities in the envelope, what was your next procedure?

A. We listed it on a piece of paper.

Q. And you showed the description of the security, the serial number?

A. I don't believe we listed serial numbers.

Q. What was the purpose of making the list?

A. Several things, as I recall, and I've been away from brokerage auditing for awhile. But one, to account for securities that were sent to First Securities from transfer agents which the transfer agent couldn't confirm to us, so we had to have some control over the fact that it takes the mail three days and we could prove that the transfer agent had mailed it before the end of the year.

Another one is to try to account for these differences in customer confirmation where the customer says, "I mailed something to First Securities on December 30th," we could see that they didn't get it till January 2nd.

Q. You say that you are no longer active in brokerage audits. When did you cease to be active?

A. In terms of having any close contact with them, it must be at least ten years.

Q. Are you now in a higher supervisory level?

A. No.

Q. You are now responsible for some other line of business?

A. Yes.

Q. What line of business are you now responsible for?

A. Manufacturing.

Q. If there were any checks included in the mail did you examine them?

A. I don't remember.

Q. Do you recall whether you listed the checks, too?

A. I don't believe we did.

Q. If there was any correspondence did you read the correspondence?

A. I don't know.

Q. Do you recall what your instructions were to your subordinates?

A. I don't believe that we had instructions to read that correspondence.

Q. So you didn't pass on any such instructions to read correspondence?

A. I don't believe so.

Q. So if a customer wrote in and said, "Why haven't I received my hundred shares of General Motors that I bought three months ago," you would not read or note such a letter?

A. That's right.

Q. How many days in succession did you get the mail and go through the routine which you have just described?

A. Either two or three.

Q. About how long after December 31st did you begin the audit?

A. On the day, December 31st.

Q. You began it December 31st?

A. Yes.

Q. Was that your standard practice in connection with brokerage house audits, that you would begin the audit on the last day of the fiscal year?

A. The last day or the day before the last day.

Mr. Bridgman: This, of course, was during the years he was connected with the audit.

Mr. Lassers: Yes, I understand.

Mr. Bridgman: Just as long as we agree to that.

Mr. Lassers: Q. Is that a practice which you follow in connection with your other audits?

The Witness: No.

Q. But that was Ernst & Ernst's policy for brokerage houses?

A. On First Securities.

Q. Was it standard with respect to the audits of other brokerage houses that Ernst & Ernst audited?

A. I believe so.

Q. Was it the standard practice on the other brokerage houses for which you were the manager or supervisor of the audit?

A. Yes.

Q. Are there any regulations of public bodies that you know of that require this, SEC regulations, et cetera?

A. Members of the New York Stock Exchange were required to start their audit on the audit date. Their audit was required to be started on the audit date or the day before, as I remember, one of the two.

Q. What about members of the Midwest Stock Exchange?

A. They were not.

Q. Then after the list of the securities was prepared, then what was done with the mail?

A. It was turned over to the person who was responsible for distribution.

Q. Was this somebody who worked in the cage?

A. No, it shouldn't have been, and I honestly don't remember who was doing it at First Securities in those days, but it should have been somebody outside the cage.

Q. That person had responsibility then for pulling out securities and checks and turning them over to the cage?

A. Yes.

Q. Under the terms of your engagement with First Securities, did you have an obligation to prepare and certify to a balance sheet?

A. Yes.

Q. What about a profit and loss statement?

A. I don't remember.

Q. When you say you don't remember, you don't remember as to the terms of your engagement with First Securities?

A. That's right. Most brokerage engagements did not require a profit and loss statement. I don't remember whether First Securities was an exception to that or not.

Q. Have you read the affidavit of Roy Campbell?

A. No.

Q. That was filed in this proceedings?

A. No.

Q. I would like to show you the affidavit of Roy E. Campbell dated December 6, 1972, and ask you to read either the entire affidavit or at least Paragraph 7 through the end, starting on Page 4.

Mr. Bridgman: Read it all.

The Witness: Hope you don't expect me to remember it word for word.

Mr. Lassers: Q. As part of your audit, did you inquire of anybody at First Securities regarding the procedures for handling the mail?

A. I don't believe so. Let me take that back. We would have liked to have securities received outside the cage. That's my recollection.

Q. Was that part of the standard procedures that were recommended by Ernst & Ernst?

A. I don't remember.

Q. Well, when you say this is something you would have liked, by you you mean Ernst & Ernst, right?

A. That's my recollection, but it could be incorrect.

Q. Was such a suggestion embodied in some kind of firm manual?

A. I don't know. I don't remember.

Q. Was there a firm manual that related specifically to the audit of stockbrokers?

A. I don't believe so.

Q. Where did you as a manager or supervisor get your instructions from as to the steps that were expected of you?

A. This was developed through our association with that assignment over a period of years and was passed down from year to year.

Q. Prior to becoming a supervisor, did you work with some other brokerage house audits as a junior?

A. Yes.

Q. So that you learned from your manager or supervisor?

A. Right.

Q. And then you carried over the same procedure. Nobody handed you a book that said, "This is firm policy on brokerage house audits."

A. That is right.

Q. Now when you say that you liked to have the securities come to somebody outside the cage, was this a point that you customarily asked about when you went in on your audit?

A. I don't remember.

Q. Is this a procedure which you simply observed and then noted?

A. I don't remember.

Q. Were you aware of the practice that several employees went over to pick up the First mail at the First office?

A. No.

Q. Were you aware of the practice at First Securities, in Paragraph 8 of Campbell's affidavit, were you aware of the procedure set out in Paragraph 8 of the

affidavit that all mail bearing an individual's name on it would be placed on the individual's desk to be opened by that individual?

A. I presume so.

Q. Did you become aware of it by observing it done while you were on the premises?

A. That would be normal.

Q. Did you inquire of Mr. Campbell as to such a procedure?

A. No, because it would be normal.

Q. Were you aware that Leston Nay had requested that no person other than himself open mail addressed to him personally or his attention?

A. No.

Q. Did you inquire of Nay whether he had given any special rules regarding the handling of mail?

A. Not that I recall.

Q. Did you inquire of Campbell?

A. Not that I recall.

Q. Or the mail clerks?

A. Not that I recall.

Q. Were you aware of the fact that as related in Paragraph 8 of the affidavit, when Nay was out of town for vacation or for business purposes he left instructions with Ms. Ryan to hold all his mail until he returned to the office?

A. I was not aware of those instructions, but I wouldn't have been surprised by them.

Q. Prior to this deposition now, were you aware of such a requirement or rule laid down by Nay?

A. No.

Q. Was the mail check that you described for the first day continued then in substantially the same form on the second or third days of your audit?

A. Yes.

Q. And thereafter, although you were working on the premises, you did not make any check of the incoming mail?

A. That is right.

Q. Did you ever have any occasion to discuss questions of internal controls with Nay?

Mr. Bridgman: The only objection is as to the meaning you have of the term internal control, so I would object to the question as to its term unless we can identify and define what is meant.

Mr. Lassers: Q. Do you know what the term internal controls means, Mr. Crockett?

Mr. Bridgman: In so far as what your understanding of that term is.

Mr. Lassers: Q. Why don't you give us a definition of internal controls?

The Witness: The internal controls are the procedures set up to safeguard the assets of the company and the assets that they're holding for others. That's it.

Q. Does it include procedures to be sure that all liabilities of a company are reflected in the books of the company?

A. I would consider that an accounting procedure rather than an internal control procedure.

Q. Well, did your examination and audit of First Securities include a review of their accounting procedures?

A. Yes.

Q. Now in light of your definition of the term internal controls, let me add to it now accounting procedures, did you ever have occasion to discuss with Leston Nay these matters?

A. Surely.

Q. Do you recall when the earliest such discussion took place?

A. No.

Q. Do you recall one particular topic that you discussed with him?

A. No, I recall none of the topics of that conversation or conversations.

Q. Do you recall any discussions with Campbell on the same topic?

A. I'm sure that Campbell was present at any discussions that we had with Nay on this subject.

Q. Do you recall if you had any questions about these matters, did you take them up with Nay directly or did you go to Campbell?

A. Might go to Campbell by himself.

Q. Then would Campbell invite Nay in to the discussion?

A. After we had resolved the situation, it would be usual for us to outline the situation to Nay so that he knew about it.

Q. Do you recall any specific matter that you took up with Campbell?

A. No.

Q. Would you have gone to anybody else in First Securities to discuss these matters?

A. No.

Q. Do you recall any correspondence from Nay or these matters?

A. I don't recall any correspondence.

Q. Do you recall any correspondence from Nay or Campbell on these matters?

A. No.

Q. Do you recall following up on any suggestions that you had made?

A. I don't recall these suggestions that were made or any followup.

Q. Directing your attention now to the annual audit, that, of course, occurs once a year. In addition to that, did you make a surprise audit?

A. No.

Mr. Bridgman: This, of course, is during the years stated in the affidavit.

The Witness: Right.

Mr. Lassers: Yes.

A. We did not in those years.

Q. At present there is a requirement for surprise audit?

A. Yes.

Q. Do you recall when the surprise audit rule was adopted?

A. No, I don't.

Q. Was it after 1957?

A. I'm sure it was sometime after.

Q. Were you ever asked to come in to make a surprise audit?

Mr. Bridgman: On First Securities?

Mr. Lassers: Yes.

The Witness: Not during those years. I have a recollection in a later year, and I don't remember whether it was coincident with the new rule or whether it happened before the rule was adopted, that we were asked to make a surprise audit.

I suspect it was when the rule was adopted, and I would guess that that was probably toward the end of my career in brokerage accounting ten years ago or thereabouts.

Q. Is this a rule of the Midwest Stock Exchange?

A. It was a Midwest Stock Exchange rule that precipitated this, yes.

Q. Are you familiar with the differences between a surprise audit and the annual audit that was done on First Securities?

A. No, except that they didn't know we were coming in.

Q. When you say they didn't know you were coming in, you mean that you showed up literally at nine o'clock one morning and said, "Here we are"?

A. I believe so.

Q. During the period of time 1952 to 1957, did you have the responsibility for signing the certificate to the balance sheet?

A. No. That had to be signed by a partner.

Q. Did you have responsibility to take the documents in to a partner and indicate to him that this was an appropriate document for him to sign?

A. It's hard for me to answer the question the way you asked it. It was my responsibility to make sure that the examination was done in such a fashion that somebody could eventually sign it.

Q. After you had satisified youself, did you prepare any memoranda, let us say, addressed to a partner, which would say, "This audit is completed. The certificate may now be signed."

A. I've got to remember our procedures in those days. I believe there was a preprinted form that I had to sign that in effect said what you just suggested what I should have said or might have said.

Q. Was the signing responsibility assigned to one particular partner on the First Securities audit?

A. No. As a matter of fact, any partner can sign it.

Q. Was that partner expected to review it?

A. Only to read the document which said that the audit had been done in accordance with auditing standards.

Q. This preprinted form, he just had to read that—

A. Look at the report and sign it.

Q. And that was it. Then he relied entirely on you that this was an appropriate document for him to sign?

A. Yes, although we also have an internal review department which looks at that in between me and the partner.

Q. The internal review department also consisted of partner s of the firm?

A. No, in those days, no.

Q. In the internal review department, were they divided up by specialists?

A. No.

Q. They were just general CPA's who reviewed anything that came along?

A. Yes.

Q. Nothing special about the brokerage client. At any time did you suggest in your preprinted form that Ernst & Ernst should note an exception to its report?

A. I don't rceall ever having done that.

Q. At that time you devoted all your time to brokerage house audits?

A. Oh, no.

Q. About how many brokerage houses were you auditing?

Mr. Bridgman: This is again between 1952 and 1957?

Mr. Lassers: Yes.

The Witness: Four five.

Q. Among those four or five is this one of the smaller ones?

A. Yes.

Q. Were the others substantially larger than First Securities?

A. No. I now recall a smaller one. I can recall one that was somewhat larger. Most of them were quite small.

Q. That you audited?

A. Yes.

Q. Did you audit any that were substantially larger?

A. There were no very large brokerage houses headquartered in Chicago that we audited. We participated in some New York headquartered brokerage audits which were sizable.

Q. When you say we, you mean Ernst & Ernst?

A. The group of us here in Chicago.

Q. Oh, you mean that these were firms that were based in New York but you audited the Chicago operations?

A. Right.

Q. So that you had experience then working with audits on brokerage houses that were much, much larger than First?

A. Yes.

Q. Does the size of a brokerage house have any bearing on the internal controls that are in force?

A. Yes.

Q. What is the bearing of size on internal control?

A. Very, very small firms would have difficulty segregating duties between the person who handles securities and, let's say, the person who handles cash.

Q. Now where do you put First Securities in this category?

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A. Not very small, but certainly small.

Q. Are there any other factors that make internal control difficult for the small office besides the one you just mentioned?

A. Not that I can think of.

Q. Are there any other functions that were segregated or divided up among several people in a large house that were performed by one employee in First Securities?

A. I'm sure there were.

Q. Were there any functions that you can recall that related to internal control, that had a bearing on internal control?

A. Well, not specifically.

Q. Did you know that Nay owned almost a hundred per cent of the stock of First Securities?

A. Yes.

Q. Does the fact that a single person owns substantially all the stock of a brokerage house have any bearing on internal control?

A. No.

Q. Do you recall whether or not First Securities used prenumbered receipts for securities received from customers?

A. No, I do not.

Q. Do you recall any discussions with Nay with regard to the use of prenumbered receipts?

A. No.

Q. Any discussions with Campbell?

A. No.

Q. With anybody else?

A. No.

Mr. Bridgman: About prenumbered receipts?

Mr. Lassers: Yes.

Q. Do you recall ever recommending the adoption of prenumbered receipts?

The Witness: I don't recall, because I don't remember whether they had them or not.

Q. Do you ever recall any discussions with Nay with regard to the practices of turning securities over to salesmen to deliver to customers?

A. I don't recall any.

Q. How about any such discussions with Campbell?

A. No.

Q. Do you know whether or not Nay ever delivered securities to customers?

A. I don't know.

Q. Did you ever ask Nay whether he did?

A. I don't know.

Q. Do you ever recall asking Campbell whether Nay delivered securities to customers?

A. I don't know.

Q. Now what about cash received, cash or checks received from customers, do you recall whether under First Securities' system if a customer sent in a check, did he receive a receipt for the check?

A. I certainly don't recall.

Q. What about cash?

A. I don't recall.

Q. Do you recall any discussions regarding the use of prenumbered receipts for cash or checks?

A. I don't recall.

Q. And I take it that your answer is you don't recall any such discussions with Nay?

A. That is right.

Q. Or with Campbell?

A. Right.

Q. Or with anybody else?

A. Right.

Q. Do you recall any discussions with Nay regarding the advisability that a receipt given by a salesman should bear a notation that it was a temporary receipt to be followed up by an official receipt?

A. No.

Q. And I take it you don't recall any such discussion with Campbell?

A. No.

Q. Or any recommendations along those lines?

A. No.

Q. Did Nay himself have access to the cage?

Mr. Bridgman: While he was there? I object to the question, access. I don't know what that means.

Mr. Lassers: 1952 to 1957, yes.

The Witness: Access, could he go in there?

Q. Could he go in the cage?

A. Yes.

Mr. Lassers: Would you please mark these documents as Crockett exhibits. Exhibit No. 1 is an answer to a financial questionnaire dated December 31, 1954. Exhibit No. 2 is the same for 1955. No. 3 is the same for 1956 and No. 4 is the same for April 1, 1957.

(Documents marked as requested.)

Q. I now show you Crockett Exhibits No. 1 to 4, which were Xerox copies of documents which I examined at the offices of Baker & McKenzie, and ask you if you can identify these as part of the X-17 (a) reports for the fiscal years ended 1954, 1955, 1956, and 1957.

A. I can't tell whether these are final or not because there's writing on them, but it looks like a form, it certainly is a Form X-17(a)5 which was prepared for First Securities. Whether it's final, I don't know.

Q. This appears to be the customary instruments and forms?

A. Yes, without our opinion.

Q. Are you familiar with the National Association of Securities Dealers?

A. I know there is such an organization.

Q. Are you familiar with its rules and regulations?

A. No.

Q. Were you aware of the fact that it had rules and regulations?

A. I suppose I was.

Q. Have you ever seen a copy of the rules and regulations?

A. I don't recall.

Q. As part of your audit, did you investigate compliance with NASD rules and regulations?

A. No.

Mr. Bridgman: Back in 1952 to 1957?

Mr. Lassers: 1952 to 1957.

The Witness: No.

Q. More specifically, were you familiar with a Rule 27(c) that related generally to a requirement of maintaining a log of all incoming correspondence and outgoing correspondence?

Mr. Bridgman: I have an objection preliminarily. There is no proper foundation laid to show the applicability of this rule or any rule under the NASD to the type of audit and the type of accounting procedures that are dealt with in this case, so it is irrelevant and immaterial, but the witness may answer.

The Witness: Did you say I could answer?

Mr. Bridgman: Sure.

The Witness; No.

Mr. Lassers: Q. During the period 1952 to 1957, were there any changes made, to your knowledge, in the First Securities system of internal control?

A. I don't recall any specific changes.

Q. Do you recall any specific changes in their accounting procedures?

A. I don't recall any changes.

Q. Did you ever discuss with any official of the SEC any weaknesses in the system of internal control accounting procedures at First Securities?

A. I don't think so.

Q. Or did you ever report any such weaknesses to anybody at the SEC?

A. No.

Q. How about the NASD?

A. No.

Q. Midwest Stock Exchange?

A. No.

Q. Any of your superiors at Ernst & Ernst?

A. I don't recall what I reported. I presume there were some comments made.

Q. Anything that stands out particularly in your mind?

A. No.

Q. Were you aware of the fact that Nay committed suicide?

A. Yes.

Q. When did you learn of that, about the time it happened?

A. I was in Colorado at the time.

Q. You saw it in the newspaper?

A. I think one of my partners told me and I don't know where he heard it or when.

Q. Are you aware of a receivership proceedings now in the Federal Court with respect to the affairs of First Securities?

A. Well, I know there is litigation. I'm not specifically aware of receivership or whatever.

Q. You are aware of the fact that there is litigation pending other than the suit in which we are now taking this deposition?

A. No, I'm not.

Q. You are aware only of this suit?

A. Yes, that's all.

Q. Did anybody ever apprise you of the fact that a group of claimants asserted that they had been swindled in an escrow scheme?

A. Yes.

Q. When did you first learn of that?

A. Two, three years ago, I suppose.

Q. Was that told to you by somebody in Ernst & Ernst?

A. Probably.

Q. I am referring to the proceedings in the United States District Court for the Northern District of Illinois entitled SEC against First Securities Company of Chicago, case No. 68-C-1053. You are not aware of that proceeding?

A. I have no familiarity with the specific proceedings. I couldn't tell you the name of this one.

Q. Are you aware of the fact that a claim of a Ms. Nora Moyer has been allowed in the receivership proceedings for approximately $175,000.00?

A. I'm not aware of that.

Q. Did you ever hear any discussion from anyone about the Nora Moyer claim?

A. Never.

Q. Until I just told it to you this morning?

A. Never heard the name before.

Q. How about a claim for Ms. Eleanor Schueren for about $17,000.00?

A. I'm not aware of that.

Q. How about a claim for the Union Bank & Trust Company of Helena, Montana, for about $394,000.00?

A. No.

Q. Did anybody ever tell you at any time that claims, apart from the names, that claims had been allowed against First Securities Company in favor of First Securities customers which were not refleected on the First Securities Company's books?

A. No.

Q. In no way, shape, or form?

A. No.

Q. Now after the Nay suicide, did you participate in any conferences at Ernst & Ernst with regard to the First Securities audits?

A. No.

Q. Do you recall whether there were any such conferences?

A. I don't recall. I didn't have any personal knowledge.

Q. Did anybody at Ernst & Ernst ever come to you to discuss the claims of the escrow claimants?

A. No.

Q. Did anybody from Ernst & Ernst ever come to you and ask you whether you had ever heard of the escrow claims?

A. No.

Q. Was there anything that you recall in the way of a post mortem of Ernst & Ernst practices with respect to the First Securities audits?

Mr. Bridgman: I have an objection as to what is meant by post mortem. I have no idea what that means.

Mr. Lassers: Q. Do you understand the question, Mr. Crockett?

The Witness: I think I can answer it.

Mr. Bridgman: Do you know what post mortem means, what he means by it?

The Witness: Well, I don't know.

Mr. Bridgman: Ask him.

The Witness: What do you mean?

Mr. Lassers: Q. By post mortem I mean whether you ever sat down with anybody at First Securities—

A. At First Securities?

Q. I am sorry, at Ernst & Ernst, sat down and said, "Well now, this and this were our procedures when we audited First Securities. Let us now review those procedures to see whether they should be changed in any respect."

A. I did not, nor was I involved in any such review.

Q. Do you know whether there were any such sessions?

A. I don't know.

Q. Did anybody ever write to you about any such procedures or post mortems in the sense I just described?

A. No.

Q. To your knowledge did Ernst & Ernst make any changes in its auditing procedures as a result of First Securities?

A. Not to my knowledge.

Q. The affidavit that you signed, was that prepared by your counsel?

A. In cooperation with him. As a matter of fact, many of the words in there are mine.

Q. Did your counsel prepare the first draft?

A. I think so.

Q. Was that in cooperation with Mr. Kist?

A. Mr. Kist and I did not cooperate in any fashion, but I think that the words ended up being quite similar.

Q. Was your affidavit prepared first?

A. I don't know.

Q. Or Mr. Kist's?

A. I don't know. I think about the same time, but I don't know that.

Q. Is your counsel Mr. Berner?

A. Yes.

Q. Mr. Robert Berner, the gentleman sitting there?

A. Yes.

Q. He prepared the first draft?

A. That's my recollection.

Q. And then he sent it over to you?

A. Yes.

Q. And you reviewed it?

A. Yes.

Mr. Bridgman: I certainly have an objection to the materiality or relevancy of this. Go ahead.

Mr. Lassers: Did you make any changes?

The Witness: Yes.

Q. Were your changes incorporated?

A. Yes.

Q. And you signed it?

A. Yes.

Q. In your audit of First Securities during 1952 to 1957, did you customarily look at the minute book?

A. Yes.

Q. What was the purpose of your minute book examination?

A. To look for anything in the minute book reflecting the actions of the Board which might have some bearing on the financial statements.

Q. Such as?

A. Dividend payments.

Q. Anything else?

A. They might discuss litigation, might approve salaries, might grant bonuses, might give stock options.

Q. Do you recall finding any such items?

A. I don't recall.

Q. Do you recall any specific items at all in the minute book?

A. No.

Q. Do you recall anything in the minute book that would indicate that there were any differences of opinion among the Directors on any topics at all?

A. I don't recall them.

Q. Was Mr. Campbell a Director during your period?

A. I don't know. I don't know whether he ever was a Director.

Q. Do you recall whether Nay was a Director?

A. Yes.

Q. He was. Do you recall how many Directors there were?

A. No.

Q. Do you recall the names of any of the other Directors?

A. I remember a name, Van Camp.

Q. Any other name?

A. Seems to me there was a fellow named Smith. His first name escapes me.

Q. Were either of these people whose names you mentioned employees of First Securities?

A. Yes.

Q. To your knowledge were any of the Directors not officers or employees of First Securities?

A. I don't recall.

Q. Did you ever talk to any of these other Directors?

A. In the course of the examination, certainly.

Q. But only in their capacity as employees?

A. Yes.

Q. You never spoke to them in their capacity as Directors, did you?

A. It's hard for me to separate the two. They were Directors.

Q. All right. But did you ever ask them about any matters that went on in Directors meetings?

A. No.

Q. Did you ever ask them whether, for example, whether on such and such an issue did they vote the way Nay wanted them to vote?

A. No.

Q. All the discussions that you recall with these people related to their work as employees, is that right?

A. Yes.

Mr. Lassers: That is all.

(DEPOSITION CLOSED)

State Of Illinois)
County Of Cook) SS

I, Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, do hereby certify that Newell Crockett was by me first duly sworn to testify the whole truth, and that the above deposition, recorded stenographically by me, constitutes a true and complete transcript of the testimony given by said deponent;

That the deposition was taken at the time and place indicated above, and that the parties were represented by counsel as shown.

In Witness Whereof I have hereunto set my hand and affixed my seal of office at Chicago, Illinois, this 9th day of April, 1973.

/s/ Alberta R. Buster

IN THE UNITED STATES DISTRICT COURT

* * (Caption—Nos. 71 C 454 and 71 C 1204) * *

The deposition of John Walsh, taken before Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, at Suite 4105, 135 South LaSalle Street, Chicago, Illinois, on Tuesday, April 3, 1973 at 2:30 P.M.

Present:

Mr. Willard King,
Mr. Willard J. Lassers,
Mr. Donald L. Vetter,
appeared for the Plaintiffs;
Messrs. Baker & McKenzie,
By Mr. Robert L. Berner and
Mr. Thomas F. Bridgman,
appeared for Ernst & Ernst.

Mr. King: This is the discovery deposition of John F. Walsh, taken pursuant to notice.

JOHN WALSH, having been first duly sworn, was examined and testified as follows:

Examination By Mr. King.

Q. Will you state your name for the record, Mr. Walsh?

A. My name is John Francis Walsh.

Q. Where do you live?

A. 9440 South Winchester in Chicago.

Q. You are the same John F. Walsh who gave an affidavit on behalf of Ernst & Ernst in this case, are you not?

A. Yes, I am.

Q. You used in that affidavit the term accounting control, did you not?

A. That might have been part of a term that I used.

Q. What was the full term?

A. Internal accounting control.

Q. What does that term mean, Mr. Walsh?

A. Well, the system of internal accounting control is the system that's inherent in the procedures of a company to prevent it from making errors in part of its normal routine.

It's a system of check of one procedure to another which may help management be assured that there aren't material omissions or errors in the work that is involved.

Q. In other words, internal accounting control refers to the procedures taken by an auditor to assure the auditor that the books and records of a securities broker contain a record of all its transactions?

Mr. Bridgman: I have an objection to that. I believe he has already given his answer as to what the term means to him, and it speaks for itself on the record.

Mr. King: Q. Will you answer?

Mr. Bridgman: Do you understand the question he just asked?

The Witness: Could you repeat the question?

Mr. King: Would you read him the question?

(Record read as requested.)

A. No, sir. I am answering that no.

Q. Why is that statement not correct?

A. Because internal controls are the procedures of people in the company, and they have nothing to do with procedures of the auditor.

Q. Doesn't the auditor in making a brokerage audit examine the system of internal control?

A. That's correct.

Q. For what purpose?

A. As part of an audit he examines the system of internal control as a basis for limiting any test that he might make of the items included in the scope of his audit. That is the primary reason for this.

Q. Does not internal accounting control refer to the steps taken by an auditor to assure the auditor that there are no unrecorded transactions through a broker?

Mr. Bridgman: Same objection including the form. The form is improper. I have the same objection as before as to the witness's answer as to his definition and testimony regarding the term used.

Mr. King: Q. Will you answer, please?

Mr. Bridgman: If you can.

The Witness: My answer is the same as before. Internal control is not a procedure of an auditor.

Mr. King: Q. The auditor has to assure himself that internal account control exists, does he not?

Mr. Bridgman: I have an objection to the form of that question. Go ahead.

Mr. King: I object to counsel coaching the witness by gestures or by words.

Mr. Bridgman: Are you referring to me?

Mr. King: Yes.

Mr. Bridgman: I haven't done that.

Mr. King: I observed you doing that.

Mr. Bridgman: You observed incorrectly.

The Witness: Will you repeat the question?

Mr. King: Would you read him the question?

(Record read as requested.)

Mr. Bridgman: An additional objection would be to the fact of the witness's prior definition of the term internal accounting controls.

The Witness: An auditor can make an examination of accounts without the existence of internal control in those accounts.

Mr. King: Q. Does an auditor of a brokerage firm make the examination of that brokerage firm without the existence of internal accounting control?

Mr. Bridgman: I have the same objection. In addition, there is no time involved in the question.

Mr. King: Q. Will you answer?

The Witness: The auditor is to make a review of the system of internal control. He can find that there is none.

Q. Are you acquainted with Mr. Jerry Hooker, the auditor for Ernst & Ernst, who has previously testified in this case?

A. Yes, I have met Mr. Hooker.

Q. Do you disagree with this testimony of Mr. Hooker:

"Q. This letter states in the next to the last paragraph on Page 2 that the essential of internal accounting control is a system which gives assurance that all transactions are recorded in the accounting record does it not?

A. Yes.

Q. Do you agree with that statement, Mr. Hooker?

A. Yes."

Mr. Bridgman: I am sorry, have you finished the question?

Mr. King: Yes.

Mr. Bridgman: My objection to the question is that it is highly improper to pose a question of this witness to comment upon the conclusions reached or credibility of some other witness.

Apparently, counsel is reading from transcript of the deposition and asking this witness to comment upon testimony made by another witness, and on that basis I object to the question and I instruct the witness not to answer that question in its present form.

Mr. King: I would like to note on the record that this witness is not a fact witness but an opinion witness, and that hundreds of cases have held that it is improper to restrict the cross examination of any witness who is offered not as a fact witness but as an opinion witness, and it is particularly improper where the witness has produced an affidavit in support of a motion for summary judgment, which affidavit is based utterly, completely, and entirely upon the opinion of that witness.

Mr. Bridgman: I respectfully disagree with the entire statement made by Mr. King for the reason that the affidavit contains factual terms in addition to an opinion of the witness.

The witness is here to answer any and all questions put to him in proper form regarding all facts in his knowledge as to what he did, what he examined, the basis of any opinion he has, and the opinion itself.

I further object to the characterization of the witness by Mr. King as cross examination. This is not cross examination of a witness. There has been no direct examination of this witness and he is called here by Mr. King on behalf of his clients to interrogate the witness.

He certainly does not qualify as an adverse witness under Rule 46(b).

Mr. King: Q. You said in your affidavit that you examined all of the records of Ernst & Ernst with respect to its audits of First Securities Company, did you not?

The Witness: Audits of First Securities? I think I did not. I stated what, sir? Please state that again.

Mr. Berner: Would you like the question repeated, John?

The Witness: Yes.

Mr. King: Would you read the question?

(Record read as requested.)

The Witness: I don't think I did state that.

Mr. King: Q. What did you state in your affidavit with respect to the records that you had examined?

A. I stated that I reviewed and am familiar with all such records and documents relating to the 1967 audit of First Securities and reviewed audit programs and calendars provided for the audits of First Securities for the years 1960 through 1966.

Q. Those records were quite voluminous, were they not?

Mr. Bridgman: I object to the characterization of voluminous. I don't know what that means.

The Witness: Not particularly.

Mr. King: Q. How much time did you spend in the examination of those records?

A. About a day and a half.

Q. Did you examine the file of Ernst & Ernst on the investigation made by its head office after Nay's suicide?

A. I did not.

Q. Did you ever read Nay's suicide letter?

A. No. I did not.

Q. You were not aware that Nay stated in that letter that First Securities Company was bankrupt because of his thefts, were you?

Mr. Bridgman: I have an objection. The witness has already stated he did not read the letter. This makes it impossible for him to answer the question.

The Witness: I did not read the letter.

Mr. King: Q. Did you read the newspaper reports of Nay's suicide?

A. Possibly the headline. Yes, I was aware that Mr. Nay committed suicide, possibly by reading the newspaper.

Q. Were or were you not aware that Nay stated in his suicide note that First Securities Company was bankrupt because of his thefts?

Mr. Bridgman: Same objection as previously stated. The witness has testified he never read the letter.

The Witness: I didn't read the letter. I don't recall hearing that or reading that in the newspaper report.

Mr. King: Q. Are you aware that Nay concealed his thefts from Ernst & Ernst for more than twenty years?

Mr. Bridgman: I have an objection to the form of that question, instruct the witness not to answer. The question is highly improper in form, certainly beyond the parameters of this deposition as I understand Judge McMillan's ruling in regard to these depositions and tneir purpose.

Mr. King: I insist that the question is pertinent to the opinions that the witness has given.

Mr. Bridgman: I think they are not.

Mr. King: Q. Do you refuse to answer the question in accordance with counsel's instruction?

The Witness: I do.

Mr. Bridgman: On advice of counsel.

The Witness: On advice of counsel.

Mr. King: Q. Are you aware that Nay's principal means of concealing his thefts was his rule that mail addressed to the company for his attention should not be opened by anybody but him?

Mr. Bridgman: Same objection and the same instruction to the witness. The question is highly improper.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: On advice of counsel I refuse to answer.

Q. You based your opinion in this case on the affidavit of Roy Campbell, did you not?

Mr. Bridgman: Same objection. The opinion is not based upon the affidavit. The opinion is based upon all of the material contained in the affidavit for which the witness is here for proper interrogation, and the question itself is highly improper.

Mr. King: I object to counsel coaching the witness.

Mr. Bridgman: I object to Mr. King's statement of coaching. I am not. I am making a proper objection. If the question were proper it could be answered.

Mr. King: Will you read him the question, please?

(Record read as requested.)

The Witness: I read Mr. Campbell's affidavit.

Q. And you mentioned it as part of the basis for your opinion, did you not?

Mr. Bridgman: I object to the question. What is stated in the affidavit is the basis upon which he predicated his opinion, including exactly what was said in the affidavit, which obviously speaks for itself.

The Witness: It was one of the items I read and included there on which I based my opinion.

Mr. King: Q. Did you examine Campbell's sworn testimony before a Federal Master, Charles M. Bane?

A. Not unless it is that affidavit.

Q. Did you read Campbell's testimony that Nay was adamant about his mail being opened by anyone but him?

Mr. Bridgman: May I have the question include where that testimony supposedly is deposited so we can identify its source for the witness?

Mr. King: Before Master Charles M. Bane.

Mr. Bridgman: I believe the witness has stated he did not recall reading that testimony.

The Witness: Unless it was in that affidavit I did not read any such testimony.

Mr. King: Q. You read nothing of Campbell's testimony except what is contained in his affidavit presented in this case, is that correct?

A. That is correct.

Q. Have you ever read the opinion of the United States Court of Appeals in the—

Mr. Bridgman: May we have the case identified by name and caption so we can identify it?

Mr. King: The case is SEC against First Securities Company.

The Witness: No, I did not.

Q. Are you aware that the opinion of the Circuit Court of Appeals is based on Nay's rule that only he could open the mail?

A. No, I'm not.

Mr. Bridgman: The witness has testified—

The Witness: I am not aware of the ruling.

Mr. Bridgman: He is not aware of the ruling, he has not read the opinion.

Mr. King: He has answered my question.

Mr. Bridgman: And he answered the previous question, also.

Mr. King: Q. You discussed your affidavit with whom before you signed it?

The Witness: With whom? I discussed it with Mr. Berner, I discussed it with some of my partners.

Q. Which?

A. Harry Weyrich.

Q. Any other partners you discussed?

A. And Mr., I possibly discussed it with Mr. Russ Wende of our Chicago office.

Q. Where is the head office of Haskins & Sells located?

A. In New York City.

Q. Did you discuss your affidavit with anyone at that office or from that office?

A. Yes, Mr. Weyrich in our executive office.

Q. What is his title?

A. He's a partner in the firm.

Q. Did Mr. Berner tell you that Roy Campbell had testified in the First Securities case that Ernst & Ernst never asked him any question which would require the divulgence by him of Nay's restrictions about opening the mail?

Mr. Bridgman: I have an objection to the question and instruct the witness not to answer that. It is highly improper.

Mr. King: Q. Do you refuse to answer in accordance with your counsel's instructions?

The Witness: I refuse to answer on advice of counsel.

Mr. King: Q. Is it your position that Ernst & Ernst were under no duty to ask questions which would have disclosed Nay's rule regarding the mail?

Mr. Bridgman: I have an objection to the question, if it is a question. It goes to a matter of law outside

the expertise of the witness. It is highly improper. It is not grounds for interrogation of any discovery procedure or deposition. I will instruct the witness not to answer.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instruction?

The Witness: I refuse to answer on advice of counsel.

Q. If you were auditing a brokerage firm today, would you ask questions which would divulge Nay's rule about the mail?

Mr. Bridgman: Same objection. instruct the witness not to answer. We are not concerned with what is done today. We are concerned with certain specified dates, none of which have been included in any question directed to this witness today.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: I refuse to answer on advice of counsel.

Q. Practically all of the large national auditing firms have been sued under the provisions of the Securities Act, isn't that true?

Mr. Bridgman: I have an objection to that. It is obviously quite irrelevant and immaterial.

Mr. King: Do you instruct him not to answer?

Mr. Bridgman: No, I don't.

The Witness: Practically all? There have been several lawsuits against many accounting firms. I am not familiar with all of these.

Mr. King: Haskins & Sells, your firm, has been sued under these acts, isn't that true?

Mr. Bridgman: Same objection as to the materiality or relevancy of this question at all.

The Witness: Under what act?

Mr. King: Q. Under the Securities Act.

A. Well, we have been sued. As to the charges under the Securities Act, I'm not familiar with the specific charges in any ongoing case, since they didn't involve assignments that are related to my work.

Q. Haskins & Sells has been sued under the provisions of SEC Rule 10(b)5, has it not?

Mr. Bridgman: The same objection as to the lack of any materiality or relevancy in this line of interrogation at all, but the witness may answer.

The Witness: I'm not sure just under what rule Haskins & Sells has been sued. They have been sued in relation to the audits of, let's say, public companies and others. We have had several lawsuits.

Mr. King: Q. Will you give us an estimate of how many of those lawsuits there have been?

Mr. Bridgman: Same objection as to the materiality and relevancy of this line of questioning.

The Witness: I can't answer that.

Mr. King: Q. Would you say Haskins & Sells has been sued thirty times?

Mr. Bridgman: Now the witness has already answered the question. He says he has no idea of the number, wouldn't give a guess. So I am instructing him not to answer. It is highly irrelevant and immaterial.

Mr. King: Q. Will you answer?

Mr. Bridgman: If you can. I won't instruct him not to answer.

The Witness: I would believe that in the history of Haskins & Sells there have been thirty legal suits against them, as a minimum.

Mr. King: Q. Has some person from Ernst & Ernst testified or given an affidavit on behalf of Haskins & Sells in any such suits?

A. Not to my knowledge.

Q. Persons from what other auditing firms have testified or given an affidavit on behalf of Haskins & Sells in such suits?

A. I am not familiar with such affidavits or firms. I have not been involved in a suit against Haskins & Sells as a defendant, and I am not familiar with the particulars in any such suit.

Q. Have you testified or given an affidavit for Ernst & Ernst in any other suit than this?

A. No, I have not.

Q. Has any other person from Haskins & Sells testified or given an affidavit for Ernst & Ernst in any other suit than this?

A. I do not know.

Q. The national auditing firms try to help each other in their defense of suits under the Securities Acts, do they not?

Mr. Bridgman: I will object to the question and I will instruct the witness not to answer on the grounds that are obvious as well as demeaning.

Mr. King: Q. Do you refuse to answer that in accordance with counsel's instructions?

The Witness: I refuse to answer on advice of counsel.

Q. Has Haskins & Sells an errors and omissions policy so that its insurance carrier defends suit against it where it is claimed that Haskins & Sells has made any error or omission?

Mr. Bridgman: Same objection as to the lack of any relevancy or materiality.

The Witness: I am not aware of the terms of our insurance policy.

Mr. King: Q. Are you aware of whether Haskins & Sells has the same errors and omissions insurance carrier as Ernst & Ernst?

A. No, I am not.

Mr. Bridgman: Same objection.

Mr. King: Q. Were there any revisions of your affidavit filed in this case before you filed it?

The Witness: No, not that I am aware. I have only filed one affidavit.

Q. You filed it in the same form that it was originally presented to you, is that correct?

A. It wasn't final, no. I have changed language during the drafting of it.

Q. Who had to do with those changes of language?

A. I did.

Q. Who else?

A. As I said, I talked to Mr. Wende and Mr. Weyrich.

Q. Did they make any changes in the affidavit?

Mr. Bridgman: I certainly have an objection to the materiality.

The Witness: I made the only changes that were made to any draft of this. As far as I know, what was originally drafted I didn't change in substance.

Mr. King: Q. When you examined the records of Ernst & Ernst, did you examine the printed or mimeographed instructions that Ernst & Ernst gave to its auditors who actually made the audit?

A. Do you have those? I examined an audit program, yes, and a calendar which was essentially the part of an audit program.

Q. Did the instructions that you examined contain an instruction that the auditors inquire whether the employees of the firm took regular vacations and their duties were performed by someone else while they were away?

Mr. Bridgman: I have an objection unless the document which presumably Mr. King is reading from or has taken that excerpt from is shown to the witness and he can identify it to be certain that what has been read is accurately contained in the document heretofore unidentified.

I don't think it is fair to ask a witness.

Mr. King: I stand on the question.

The Witness: I don't recall.

Q. That is standard auditing procedure in the auditing of any financial institution, is it not?

Mr. Bridgman: Same objection as to the inclusion in the question of the prior question, which is highly improper, and I would instruct the witness not to answer this question.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: I refuse to answer on advice of counsel.

Q. Is it not standard auditing procedure of financial institutions to inquire whether the officers and employees take regular vacations and their duties are performed by others while they are away?

Mr. Bridgman: I have an objection unless we put a time in the question, please, as to year.

Mr. King: I stand on the question.

Mr. Bridgman: Well, I will instruct the witness not to answer the question unless there is a specific year included in the question so that the standard operating principles or procedures can definitely be delineated as to a specific period of time.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: I refuse to answer on advice of coun-

Q. Have you ever known of an audit of a financial institution where the auditors did not ask the question whether the employees took regular vacations and their duties were performed by others in their absence?

Mr. Bridgman: Same objection as to the lack of a date in the question and the relevant standard principles referred to therein.

The Witness: I have known such audits. We audit places without employees.

Q. Well, where you don't audit places without employees, have you ever known of an audit where the auditor did not ask that question?

A. Yes.

Q. What was that audit?

A. The audit—I think that question is irrelevant in an audit of a small brokerage firm. There are, I would say that it is not involved in, the question would not be asked in firms the size of Ziv Investment Company, Hickey & Company in this building, several others.

Q. Have you completed your answer?

A. Yes.

Q. The national bank examiners throughout the United States invariably ask whether the President, Vice Presidents, and employees of a bank take vacations and their duties are performed by someone else in their absence, do they not?

Mr. Bridgman: I have objection to the lack of materiality and relevancy to that question as it does not refer to the issues involved in this case in any respect, nor to any part of the affidavit filed in the case by the witness, and it is wholly immaterial and irrelevant.

The Witness: I am not aware of all the requirements of the National Bank Examiners Institute. We were con-

cerned with firms in the securities industry, and I thought your reference to financial institutions was a general statement which included those firms in the securities industry.

Mr. King: Q. Is it your position that the auditors' question of whether the officers and employees of a brokerage firm take regular vacations and have their duties performed by someone else during their absence is not an important question?

Mr. Bridgman: I object to the form of that question and certainly instruct the witness not to answer.

The Witness: I refuse to answer on advice of counsel.

Mr. Bridgman: The question has been previously asked and answered. It is improper in form.

Mr. King: Q. Is it your position that that question about regular annual vacations is no essential part of the internal accounting control?

Mr. Bridgman: Same objection. The witness has previously answered the question under the circumstances that exist in differing situations. The question has been asked and answered.

Mr. King: Do you instruct him not to answer?

Mr. Bridgman: No.

The Witness: I feel that rotation of duties and regular vacations by employees can affect, possibly enhance internal control, that the lack of such does not necessarily indicate a weakness in internal control.

Mr. King: Q. Would a national bank examiner approve on examination a bank whose President insisted that when he was away on a vacation the mail addressed to the bank for his attention should not be opened by anyone but him, but should pile up on his desk unopened until he returned?

Mr. Bridgman: I have the same objection as previously made. In addition, there is no proper foundation for asking this witness this question regarding an examination made of a bank.

It is irrelevant and immaterial to the issues in this case, and the purpose for which this deposition was supposedly to have been taken.

The Witness: Sir, as far as the bank is concerned, I do not have knowledge of the routine of national bank examiners, knowing their scopes or their purpose.

Mr. King: Q. Adequate internal accounting control requires that brokerage firm transactions and records of transactions be handled by more than one person, does it not?

Mr. Bridgman: I would object again to the characterization of what is adequate or inadequate, and the witness has previously testified at the beginning of this deposition as to what internal accounting control means to him and standard operating procedures in audits.

The Witness: Good internal control is based on many things and it often includes the separation of duties between the handling of assets and recording thereof.

Mr. King: Q. Does Haskins & Sells issue typed or printed instructions to their auditors actually making securities brokerage audit?

Mr. Bridgman: At the present time, Mr. King, or when, may I ask?

Mr. King: It includes the present time.

Mr. Bridgman: It is all-inclusive?

Mr. King: Yes.

Mr. Bridgman: I object to the question on the ground it is irrelevant and immaterial.

Mr. King: Do you instruct him not to answer?

Mr. Bridgman: No.

The Witness: At the present time we use printed audit programs to cover the general examination. All of our general examination. They can be expanded on or discarded if they do not apply.

Q. Will you produce those printed forms for our examination?

Mr. Bridgman: I think you better get an order for that.

Mr. King: Q. Do those instructions to your auditors contain an instruction that the auditor shall ask whether the employees take regular annual vacations?

Mr. Bridgman: Same objection as to irrelevancy and immateriality, and there is no time stated in the question.

The Witness: We have had several programs, internal control questionnaires throughout the years, and some do and some don't.

Q. Do those instructions include the following, which I find in the typed instructions of another national auditing firm to its accountants making an audit of a securities brokerage firm:

"Are duties and responsibilities clearly defined and unmistakeably assigned in such a fashion that no single employee, (a) has control of an entire operation, (b), has complete control over both transactions, documents, and records controlling those transactions."

Mr. Bridgman: Objection again as to materiality and relevancy of what Haskins & Sells documents contain. The additional objection that the document is only identified in general terms by Mr. King and not specifically identified as to source, nor has it been shown to the witness, and there is no date again in the question or time.

The Witness: Would you repeat the question?

(Record read as requested.)

The Witness: I think we have nothing that is so all-inclusive.

Mr. King: Q. Would you say that was a typical or untypical instruction to auditors actually making an audit of a securities house?

Mr. Bridgman: I have an objection. That is asking the witness to characterize what the instructions are or what they do. I think they speak for themselves, as does the prior answer by the witness.

The Witness: A broad statement like that I would say is not necessarily typical of what you would see in programs that I am familiar with.

Mr. King: Q. I hand you a book on audits of brokers and dealers in securities issued by a Committee on Stock Brokerage Accounting and Auditing, which I will ask the reporter to mark Walsh Exhibit No. 1 for identification.

(Document marked as requested.)

Q. Are you familiar with this document?

A. Yes, sir. It is an exposure draft of a proposed audit guide that has since been substantially revised. I sent a letter on this, commenting on this document, to Mr. Hanley of the American Institute.

Mr. Bridgman: May we have the date the document bears?

The Witness: This says Exposure Draft of July, 1971.

Mr. King: Q. You listed on Page 4 of your affidavit the literature only through the year 1967, did you not?

A. Yes, I referred to 1967.

Q. So you did not list any such document as this 1971 document, which is Walsh Exhibit No. 1, is that correct?

A. This is not an authoritative document. That has never been published and will never be published in that form.

Q. Will you turn to Page 190 of Walsh Exhibit No. 1 and read for the record Paragraph 12 on that page?

Mr. Bridgman: I have an objecton to any inquiry into the document identified as Walsh Exhibit No. 1 in view of the witness's prior answer to the prior question regarding the fact that the document has not been and will never be a published document, nor an authoritative work of any type in document form, regarding the competency.

The Witness: "Bookkeepers and margin clerks should be rotated periodically so that they are not always servicing the same accounts."

Mr. King: Q. Thank you. Have not changes been made in the auditing requirements of brokerage firms to avoid the debacle that occurred in that case?

Mr. Bridgman: In what case?

The Witness: In this? What debacle?

Mr. King: Read him the question.

The Witness: You said debacle in the case.

(Record read as requested.)

The Witness: I don't know what you refer to.

Mr. King: In the Nay case.

Mr. Bridgman: I certainly have an objection as to the form of the question.

The Witness: The debacle—I can't answer that. Will you define debacle.

Q. Have any changes been made in the auditing requirements and standards of brokerage firms as a result of the Nay case?

A. There have been changes in the auditing requirements since 1967. I have never heard them referred to as the result of the Nay case.

Q. Can you testify they were not made as a result of the Nay case?

A. No, sir.

Mr. Bridgman: I think he has already testified.

Mr. King: Q. Can you tell us what those changes were, in general?

Mr. Bridgman: I object to the immateriality and irrelevancy of any changes in any procedure subsequent to the year 1967 as being irrelevant and immaterial and inadmissible in this particular case and as to the issues between the parties, particularly as to the content of the affidavit of the witness.

The Witness: There have been changes in Rule 17(a) 5, mostly changes in reporting. Recently, now we have been required to extend our audits to the audits of operations of a broker-dealer covering the entire period from one examination to another.

There are many other reporting requirements. There's a new reporting requirement in connection with the assessments paid to Securities Investors Protective Corporation.

Back in 1968 there were changes in reporting to the SEC relating to material inadequancies in internal control that requires a statement if any material inadequacies in the system of internal control and safeguarding of securities were disclosed.

The form itself, X17(a)5, was changed several times in the period, mainly to make it more meaningful in relation to the needs of the regulatory people because of the paper work crunch of the mid-sixties.

Mr. King: Q. If you were making an audit of a brokerage house today substantially owned by one person who was its President, would you fail to ask questions which would disclose that he had forbidden anybody but himself to open mail addressed to the company for his attention?

Mr. Bridgman: I would object to the question on the ground that it refers to the present date, which is irrelevant and immaterial. It is completely speculative and conjectural, would require a guess on the part of the witness since there are not sufficient facts in the question upon which to predicate an informed opinion, and there is no proper foundation laid for the question.

Mr. King: Do you instruct the witness not to answer?

The Witness: We would make many questions, have many questions regarding the handling and recording of cash receipts and disbursementss and receipts and deliveries of securites.

Q. Have you completed your answer?

A. I have.

Q. If today you discovered such a rule about the opening of mail, would it not arouse suspicions on your part which would lead you to make further investigation?

Mr. Bridgman: Which I would again repeat the same objection as made to the previous question. The question is also improper in form.

The Witness: Sir, it's a fact of life that many of the companies we audit have people who handle cash prior to recording. We take this into consideration in the scope of our audit.

Mr. King: Q. Have you completed your answer?

A. Yes, I have.

Q. Has the Nay case led to any changes in auditing procedures of brokerage houses?

Mr. Bridgman: I object. It has already been asked and answered, but go ahead, do it again.

The Witness: There have been several changes in auditing procedures. I have not heard them attributed specifically to the Nay case.

Mr. King: Q. Shouldn't the Nay case in your opinion have led to such changes?

Mr. Bridgman: I certainly object to that question and instruct the witness not to answer. It is no way probative of any of the issues in this case. It is completely irrelevant and immaterial.

Mr. King: Q. Do you refuse to answer in accordance with counsel's instructions?

The Witness: Did you say not to answer?

Mr. Bridgman: Don't answer the question. It is ridiculous.

The Witness: I refuse to answer on advice of counsel.

Mr. King: Q. When you based your affidavit in this case in part upon the affidavit of Roy Campbell, did you observe that Campbells' affidavit refrained from stating that Nay took regular vacations?

Mr. Bridgman: I object again. The witness has testified earlier that he took into consideration the content of that particular affidavit as part of the ultimate opinion he reached, predicated on other things, also. The affidavit of Mr. Campbell speaks for itself.

The Witness: I was aware that the affidavit of Mr. Campbell said that Mr. Nay was away from the office.

Mr. King: Q. But were you also aware that it did not use the word regular vacations?

Mr. Bridgman: Same objection.

The Witness: I don't recall.

Mr. King: Q. Did you observe that Campbell's affidavit refrained from stating that Nay's duties were performed by someone else in his absence?

Mr. Bridgman: Same objection. The affidavit and its contents are filed in support of the motion and that is what has been considered by the witness. It is improper to ask him what he would not consider in the affidavit.

The Witness: I have not read Mr. Campbell's statement recently. I remember generally what was in it. There are many things that were not in it. I do recall that he mentioned that Nay was away from the office several times.

Mr. King: Q. But you do not recall the omission of the words regular vacations or the omission of the words that someone else performed his duties in his absence, is that correct?

Mr. Bridgman: Same objection to the form of the question.

The Witness: I don't recall.

Mr. King: Q. You stated in your affidavit, did you not, that it is no part of the duties of independent auditors to ascertain whether a security firm has complied with NASD Rule 27(c), which requires a member of NASD to endorse in writing on an internal record all correspondence of its registered representatives pertaining to the solicitation or execution of any securities transaction?

Mr. Bridgman: May I ask where in the affidavit that is contained, Mr. King, so the witness may refer to it as to its accuracy?

Mr. King: The witness has the affidavit before him.

The Witness: I don't think I referred to Rule 27(c).

Q. What did you refer to on that subject, NASD rules?

A. Paragraph 9, it says, "An examination by independent auditors to determine compliance with the rules and regulations of the National Association of Securities Dealers, including its rules of fair practice, is not and has never been within the scope of the regular annual audit of financial condition of an NASD member of a certified public accountant."

I agree with that statement.

Mr. Bridgman: You mean with the statement you just read?

The Witness: The one I just read, yes.

Mr. King: Q. Independent auditors are subject to law, are they not?

A Yes, sir.

Q. Have you read the two opinions of the Court of Appeals of the Seventh Circuit, on both of which certiorari has been denied by the Supreme Court of the United States, holding that a securities company was civilly liable for its non-compliance with Rule 27 of the NASD?

Mr. Bridgman: The witness has already said he hasn't read any opinions of the Seventh Circuit.

The Witness: I haven't read that.

Mr. King: Q. In making an audit you make no inquiry whether the NASD rules have been complied with, is that correct?

Mr. Bridgman: Same objection as to the time in question as to today. Irrelevant, immaterial, and no probative value to the issues in this case. The witness may answer.

The Witness: It is not part of our examination to ascertain that the broker has complied with the rules as such of the NASD.

We may inquire and ascertain that he has done things similarly, but we are concerned if the person is in violation of these rules and an examination of the NASD

would prevent them from continuing in business, which would jeopardize their existence as a going concern.

This would affect our opinion on their financial position. It is just like we are also the auditors of General Motors, and we don't inspect their automobiles to see that they meet federal emission standards.

However, if the Environmental Protection Agency was going to put them out of business, we would be much concerned in our opinion on those financial statements. It's the same thing.

Mr. King: Q. Have you completed?

A. Yes, sir.

Q. How can you testify that a financial statement fairly represents the condition of a securities broker if you have made no investigation of whether it has any liability or non-compliance with NASD rules?

Mr. Bridgman: I am going to object to the form of the question. There is no time in the question.

The Witness: Sir, we inquire, we look at the reports, we inquire of the client whether they have received, had an examination of regulatory agencies and the replies that they have received from the regulatory agency in relation to those examinations.

If they would be in jeopardy of being restricted or suspended in their business, we would be much concerned.

Mr. King: Q. You state in your affidavit, do you not, that you have examined all the files of Ernst & Ernst relating to its audits over the period from 1960 through 1967?

A. No.

Q. What is your statement on that subject?

A. It's included in my affidavit, sir, that I examined the files, the working papers in 1967.

Mr. Bridgman: May we have the page and paragraph and read it, please?

The Witness: "Ernst & Ernst has submitted to me records and documents which it has represented to me are all the records and documents retained by it with respect to its audits of First Securities in its possession prior to the commencement of these proceedings.

"I reviewed and am familiar with all such records and documents relating to the 1967 audit of First Securities and reviewed the audit programs and calendars provided for the audits of First Securities for the years 1960 through 1966."

Mr. King: Q. I show you a Xerox copy of a handwritten memorandum of Jerry M. Hooker, which has previously been marked Hooker Exhibit No. 17 for identification.

Mr. Bridgman: I might suggest that it be marked as an exhibit today, Mr. King, with today's date, so there will be no confusion in the future.

Mr. King: There will be no confusion.

Mr. Bridgman: May I ask the reporter to mark it, because perhaps I am easily confused. But I would like to have it bear today's date.

Mr. King: Q. Do you recall seeing this document?

The Witness: Yes, I am aware of its existence.

Mr. King: Counsel wanted this marked. Mark it Walsh Exhibit No. 2 of this date.

(Document marked as requested.)

Q. What is the minimum capital required for a member of the Midwest Stock Exchange?

The Witness: At October 31st or at that time?

Q. Yes.

A. It has changed over the years.

Q. What was it at this date?

Mr. Bridgman: May we have the date?

Mr. King: 1967.

The Witness: At October 31, 1967, generally it required a ratio of net capital or an aggregate indebtedness to net capital of no greater than fifteen to one. There were minimum requirments of capital I think of $25,000.00.

Q. How is that $25,000.00 computed?

A. Well, the rule is defined in Article 20 of the Midwest Stock Exchange rules. Essentially, you can approach from two ways. But you take the shareholders' equity and make certain deductions from that for assets not readily convertible into cash or illiquid assets, would at least be the non-current assets on a balance sheet.

In addition, there are rules relating to specific items, investment in securities, for instance, of common stock, referred to as a haircut of thirty per cent.

Bonds have a different percentage. U.S. government obligations have different percentages. These are deducted from the equity section of the balance sheet to come to net capital.

Aggregate indebtedness is generally the liabilities of the company, with certain exceptions that are defined in the rule.

Q. Have you finished?

A. Well, the ratio of fifteen to one is applied to see that the capital is at least 1/15, six and two-thirds per cent of this aggregate indebtedbess.

Yes, I'm finished.

Q. Did the large indebtedness of Nay at that time to First Securities Company play any part in the computation of minimum net capital of $25,000.00?

Mr. Bridgman: I would object to the characterization of the indebtedness as being large, whatever that means, as to the form of the question.

The Witness: The receivable from Nay on the records was part of the computation. I do not recall the details of the computation, although I examined them at that time.

Mr. King: Q. Did the large indebtedness of Nay to First Securities Company play any part in this computation of ratio of total indebtedness of the company to capital?

Mr. Bridgman: Same objection as to the characterization of the indebtedness as large. I object to the form of the question and that specific characterization.

The Witness: Sir, I examined the computation at the time. Why it failed to meet, whether it was the $25,000.00 or the fifteen to one, I do not recall at this time.

I remember that the deficiency, according to my computation, was approximately $9,000.00, and that was in their working papers.

Mr. King: Q. Are you familiar with the rule of the Midwest Stock Exchange that a member who has a deficiency in net minimum capital must furnish for six months thereafter each month a statement of its computation of net capital?

Mr. Bridgman: Object to the question as to the failure to include therein any specific time period and date.

The Witness: I think that rule has changed over the years, sir. They have had something along those lines, but it is not in their—well, it has not always been in their rule as such. There have been various administrative instructions relating to firms who had minimum amounts of capital.

Mr. King: Q. The court has found in the First Securities case that First Securities had debts of some $2,200,000.00. Was $25,000.00 adequate capital for First Securities Company for that indebtedness?

Mr. Bridgman: I will object to the form of the question as to what the court found. The witness has stated he has not read any opinion, and I don't know how he can give an opinion as to the queston as phrased.

There is no proper foundation for the question. It calls for speculation, guess, and conjecture.

The Witness: Sir, I am not aware of the court's opinion. I did review the computation that was based on the books and records. If there were unrecorded liabilities, they were not part of these working papers.

Mr. King: Q. What would be the net capital required for an indebtedness of $2,200,000.00?

Mr. Bridgman: Objection unless we have a time. Go ahead.

The Witness: Under the Midwest Stock Exchange rules?

Mr. Bridgman: Under the present rule.

The Witness: It would be in excess of $140,000.00, assuming these liabilities were all includable in aggregate indebtedness as defined by the rule.

There can be a large amount of liabilities excluded under the exceptions in the rules.

Mr. King: Q. Mr. Hooker states in this memorandum that he was instructed by the Vice President of the Midwest Stock Exchange not to show the deficiency in net capital of $9,000.00 under the minimum $25,000.00 because the deficiency had been corrected, does he not?

The Witness: Yes. Well, instructed, he says words similar to that. He did not believe that disclosure of the deficiency in the questionnaire was appropriate, since it had been corrected.

Q. Did you observe from the papers of Ernst & Ernst that the deficiency was corrected by Nay repaying $10,000.00 of his $84,000.00 indebtedness to First Securities?

A. I don't recall that.

Q. And did you not observe that twenty-five days later Nay again borrowed that $10,000.00 from First Securities, which he had repaid to rememdy the deficiency, isn't that true?

A. I don't recall that.

Q. Was it in accord with standard accounting procedures for Mr. Hooker not to mention this deficiency in net capital in the auditor's report?

A. As of October 31, 1967, very few statements of brokers included any note in relation to their capital requirements. It's a commonplace thing tody to mention the minimum capital required and the status of the company in the note to financial statement.

This has evolved in the last two years. I would think that you didn't find the notes in relation to the capital requirements in brokers' financial statements issued in 1967.

Q. I hand you again Wash Exhibit No. 1 and ask you to read the rule for the record that appears on Page 143.

Mr. Bridgman: I have the same objection as I previously made with regard to the use of this document, since the witness has testified that it is not and will never been published, nor will it ever be authoritative in the field.

With that objection the witness may answer.

The Witness: A violation of the applicable net capital rules as of the audit date requires footnote disclosure and may require the independent public accountant to qualify his opinion because of going concern considerations.

However, there may be situations in which the capital deficiency is corrected prior to the issueance of the in-

dependent public accountant's report. In these circumstances footnote disclosure may be adequate.

Mr. King: Q. Will you finish your answer?

A. This is an exposure draft dated July, 1971, when this footnote had become rather prevalent.

Q. In other words, is it your testimony that Hooker would not be following standard accounting procedures today in failing to record or show on his audit, but there was no rule that required him to show that at that time, is that correct?

Mr. Bridgman: I object to that question.

The Witness: If I understand your question, there was no rule for him to report the capital status in 1967, this being a rule as such, it's an audit guide and the practice became prevalent after the failure of the New York Stock Exchange Fund to protect the customers of broker-dealers, the failures of several large companies.

Mr. King: Q. When you make an audit today, the auditor opens and examines the mail for certain dates at the time of his audit, does he not?

A. He may. Generally, we do in a securities examination.

Q. When you examine the mail do you read the correspondence?

A. No, sir, not in detail.

Q. Not in detail?

A. A broker receives a large amount of mail. We are primarily concerned with securities received in envelopes, again, primarily as they are being returned from transfer agents, because of the difficulty in verifying them otherwise.

Q. Would you ignore a letter of a customer which you opened which complained about non-delivery of securities?

Mr. Bridgman: At the present time?

Mr. King: Yes.

Mr. Bridgman: That is irrelevant and immaterial. It has no probative value.

The Witness: Sir, we would be concerned on how a company handled the complaints of its customers. If something important came to our attention, we would mark it for followup.

In the mid-sixties and late sixties it was not unusual for customers to complain about deliveries, delays of deliveries of securities. There have been many studies that have stated that the securities industry had fallen behind in their work in those years.

Mr. King: Q. Do any of your brokerage clients today have a Nay-type rule regarding the mail?

Mr. Bridgman: Object to the form of the question, also the irrelevant and immaterial aspect of the question as to today's date, and it has no probative value as to the issues herein.

The Witness: A Nay-type rule? Do you mean a rule that says that no one shall open the President's mail?

Mr. King: Q. I mean a rule that says no one shall open the mail addressed to the company for the attention of the President.

A. What was the question?

(Record read as requested.)

A. I don't know of any client that has a rule that says that a person is not to get mail addressed to them. As far as a positive statement that forbids it, I don't know that any has, but I don't know of any rule that says that all the mail of every person, regardless of the addressee, is to be opened.

Q. If you found today that the President of one of your brokerage clients had a rule that mail addressed

to the company for his attention should not be opened by anyone but him, would you take any action regarding that rule?

Mr. Bridgman: The same objection as to the present time. It is irrelevant and immaterial. There is no probative value as to the issues in this case.

The Witness: The procedures that encompass the internal control in a broker-dealer, there are many of them. I would discourage a rule forbidding people from getting cash and securities and having them handled prior to recording.

We try to discourage any such handling. It's generally found that brokers object to being treated like a lock box system. A good procedure would be to have a lock box.

However, such a procedure would not prevent mail going directly to persons to whom it's addressed, and I think it's just one aspect of the problem of handling of assets prior to their recording and that it's not just one thing.

I think I would discourage not only the President from handling cash prior to recording, but anyone else. As a matter of fact, it seems in Mr. Campbell's testimony they did provide an envelope to receive checks back and that were postage due type so that they would come directly to the cashier to minimize the handling.

I believe that is a good thing. I encourage my clients to do that. I wish they all had done that.

But a rule just to prevent the President from opening mail addressed to him, surely I would remind them now that there is a situation where it is alleged that this is how these things happen.

However, I don't think that is internal control. There's much more to it in the handling of cash and securities.

Mr. King: Q. Have you completed your answer?

A. Yes, sir.

Q. Will you turn to Page 7 of your affidavit and read what your affidavit says with respect to the system of internal control of First Securities Company.

A. "In my opinion, for the years 1960 to 1967 the system of internal accounting control maintained at First Securities Company contained sufficient procedures and measures to safeguard the firm's assets, to check the accuracy and reliability of its accounting data, so that in no circumstance would the existence of a procedure with respect to mail as described above in Mr. Campbell's affidavit be relevant or determinative of the existence or lack of internal control for any purpose, including for the purposes of comments by auditors to regulatory bodies or national securities exchanges in connection with an accountant's expressions of opinion on the financial statements of a broker or dealer in securities.

Q. When you swore that the system of internal accounting control was sufficient to safeguard the firm's assets, were you aware of the liability of First Securities to Ms. Moyer for $175,000.00, which was not recorded on the books?

A. I don't know that name.

Q. And you were not then aware of the $17,000.00 liability to Ms. Schueren, which was not reported on the books?

A. I'm not aware of that name, either, sir.

Q. And you were not aware of the liability of $394,000.00 to the Union Bank of Helena which was not recorded on the books?

A. I'm not aware of that.

Q. And you did not look into the weaknesses of an accounting system which would permit those omissions, if they existed?

Mr. Bridgman: I object to that, certainly. I instruct the witness not to answer. I don't know what that question means or where these figures came from.

The Witness: I will not answer on advice of counsel.

Mr. King: Q. Do your clients use numbered receipts?

A. Some of them do, sir, not regularly.

Q. You don't regard the use of numbered receipts as esential to internal accounting control?

Mr. Bridgman: Object to the form of the question again as there is no time.

The Witness: Numbered receipts can add to a system of internal control. They are generally not used because of other reasons, administrative reasons.

This does not in any way destroy internal control.

Mr. King: Q. You stated, I think, that in 1967 you did not comment in an audit of a brokerage firm on the net capital.

A. We did not make a report, our report did not include such a comment.

Q. Would you have commented where there was a net capital deficiency?

Mr. Bridgman: I object to the form of the question as to what this witness would have done. The question is improper in form and no proper foundation has been laid.

The Witness: If such deficiency jeopardizes the going concern basis of the business, I definitely would have disclosed it and taken exception in my opinion.

Mr. King: Q. Do any of the brokerage clients which you described in your affidavit have a situation where one man owns as much as ninety-two per cent of the stock of the concern?

A. I have clients where there are sole or almost, similar situations, I would say.

Q. Do you regard the auditing of those as more difficult or less difficult than the large clients where the ownership is divided?

Mr. Bridgman: Object to the form of that question. It is irrelevant and immaterial to the issues here.

The Witness: In the case of small brokers where the internal control is not considered good, we do not limit our tests as much as the limitations that we would make on a firm with good internal control, with strong internal control. There are many shades of internal control.

Mr. King: I am not sure if I understand you.

A. Sir, you say more difficult. A large job takes much more time. Difficulty is related to time. Generally the larger brokers take more time.

Q. If I understand you, you would be more lenient on internal accounting control withh a small single ownership company than you would with a large company with divided ownership, is that correct?

Mr. Bridgman: I have the same objection.

The Witness: I don't understand your word lenient. We are not the regulator.

Mr. King: Q. Do you require higher standards of internal accounting control with a large company than you would with a small company, is that correct?

Mr. Bridgman: Same objection as to immateriality, relevancy, and probative value or the lack thereof.

The Witness: We expect internal control to be reasonable, reasonable cost, raasonable in relation to the number of people. It's a system that is provided with the employees that are necessary to conduct the operation of the business.

Therefore, we would expect the internal controls of a large firm to be more structured than those of a smaler firm.

Mr. King: Q. But in any event, would you not require as part of your duty as an auditor internal control to be adequate to safeguard the company?

A. Again, sir, we are not the regulators. We adjust our scope of our examination in relation to our findings of our review of internal control in safeguarding securities.

We report to the SEC and to the exchanges in a letter now, in recent years, and not in 1967, if we feel that there is a material deficiency in internal control.

In a very small company we generally disclose the fact that it is a very small company and that separation of duties is impractical, which is now reported to the regulatory people, and they do with it whatever they want.

Yet we still, this does not in any way change, impair our report on the financial statements of that company.

Mr. King: I think that is all. Thank you very much.

(DEPOSITION CLOSED)

STATE OF ILLINOIS)
COUNTY OF COOK) SS

I, Alberta R. Buster, a notary public within and for the County of Cook, State of Illinois, do hereby certify that John Walsh was by me first duly sworn to testify the whole truth, and that the above deposition, recorded stenographically by me, constitutes a true and complete transcript of the testimony given by said deponent;

That the deposition was taken at the time and place indicated above, and that the parties were represented by counsel as shown.

In Witness Whereof I have hereunto set my hand and affixed my seal of office at Chicago, Illinois, this 9th day of April, 1973.

/s/ Alberta R. Buster

SCHUEREN EXHIBITS 178 and 179

March 3, 1967

Mr. Loston B. Nay, President
First Security Company of Chicago
135 South LaSalle Street
Chicago, Illinois 60603

Re: Arnold Schueren Estate

Dear Mr. Nay:

On Tuesday, February 28, 1967, the Union Bank and Trust Company of Helena, Montana, was appointed Executor of the Arnold C. Schueren Estate. I am enclosing a certified copy of our appointment for your files and records.

After our appointment, the attorney for our estate and I went to visit Mrs. Schueren at the hospital. She had planned to be out of the hospital at that time, however, due to some minor complications, it was necessary for her to stay a few days longer. During our visit she told me of their long association with you and about your long personal friendship as well as business dealings. From what Mrs. Schueren has told me, I am certainly looking forward to meeting you when you are visiting her at the ranch.

As Executor it is, of course, our duty and responsibility to prepare an inventory and appraisement of all of the assets to be presented to the District Court. In that connection, of course, we must ask that you please forward to us all of the bonds, securities and assets you

BEST COPY AVAILABLE

Mr. Leston B. Nay
March 3, 1967
Page Two

hold for Arnold C. Schueren. I understand that you undoubtedly will be holding some cash generated from those assets which will give us the start on funds for the widow's allowance to be paid to Mrs. Schueren during the probate. Any detailed information you can give me along the lines of income and an explanation which will enable us to properly set up our records will be very much appreciated. In that connection, any background information that you might have or care to pass on which will help in the preparation of the tax reports, etc. will also be very much appreciated.

We assure you Mr. Nay that we are looking forward to working out any problems Mrs. Schueren might have and want to cooperate with you in any way possible. Any time I can be of any assistance, please feel free to contact me.

Sincerely yours,

Herman P. Mayer
Trust Officer

HPM:EFM

SCHUEREN EXHIBITIS 3-69 to 3-75

(Front of Envelope)

TO: DELIVER PROMPTLY

Roy Campbell of

First Securities Company of Chicago

To all authorities who will have jurisdiction

Telephone: (PILGRIM)
PI 8-5869

Park Forest, Ill.

[ON FIRST SECURITIES LETTERHEAD]

JUNE 2

to not open the office for business Monday June 3 -

Due to my thefts, the company is bankrupt -

Call Foster and retain him if you can

Call the Exchange and Ernst & Ernst -

The thefts affecting the Company are

The Schueren acct. (Union Bank of Helena - Loomis-Continental Bank.

Moyer acct -

/s/ Leston B. Nay

to the police, counsel for First Securities Company and all authorities

age 1) May 31, 1968 At Home 10 p.m.

(Campbell)
Cashier of First Securities Co.

1.) Combination of safe in my office

Right to 11 4 Times
Left to 7 3 Times
Right to 56 Twice

2.) Inner compartment of same

Right to 2 4 Times
Left to 29 3 Times
Right to 56 Twice

3.) Safety Box at Continental Bank

M 5907 (Key on my Key Ring

4.) Tax and "Escrow" File:

Right bottom double drawer of office desk

5.) Norman L Moyer, Nancy Moyer file: middle drawer of safe in office

6.) Schueren - and Estate file (Union Bank & Trust Co. Helena Montana

1.) In my brief case (on desk of my bedroom in apartment and bottom drawer of office safe.

Defalcation of Schueren's securities started in 1938 I think (whenever his first Power of Attorney to me is dated (see one of the files in bottom drawer of office safe - also see "Receipt" I issued for his securities in "safekeeping" received by Ryan Nichols & Co. from Webber Darch & Co. in June of 1942 - interest and dividends on "safe-keeping" items paid by cashier's check I bought at Continental Bank - some stocks he sent in for safe-keeping, (still in his name) are in my safety box at Continental Bank, together with his wife's securities, bought thru us, such as:Swift, Gen. Publ. Service. Etc. - other items on my monthly income statements are of course spurious.-

Real securities belonging to both accounts were sold thru City Natl. and Continental, having been used as collateral.

Same story of Norman L. Moyer's wife's securities.

Re Schueren Estate: I stalled Union Bank in Helena (Herbert Mayer) see correspondence, 'till now. I phoned him today saying, that most sec'ies are back from transfer Monday -

"Nay" securities in collateral at Continental Bank. 1) 3M Ill. Toll 3-3/4's and all Governments are property of Leon S. Marfin, 11519 Maplewood Ave., Chicago (all purchased thru us).

2.) Remaining $11 M Tolls are what is left from those originally sold to Mrs. Norman L. Moyer (see her acct.) also New York Central 4-1/2/s and El Paso Natural Gas 3-1/2's mine -- Atlas Corp. Debentures and Helene Curtis are really mine -- 3-M Ill. Toll 3-3/4 in Mrs. Nay's name are really hers -- You can trace bond numbers to last Sec'ies file -- Ill. Toll Exchange of years ago and also purchases for cash -- her account --

Narrow Operation: My wife, Eliz. W. Nay was a victim exactly like the others (list attached & also see record of receipts and interest payments in my brief case and Tax returns (Interest paid).

In addition in Mrs. Nay's safety box see my receipts for other "investments" cash in her safety box she accumulated over the years from "interest" I paid on these investments.

Her copies of Federal Tax returns were specially prepared for her - all other joint returns she signed in . . .

into blank. -

Important - Mrs. Norman L. Moyer is almost 80 years old, frail and a little senile. - She is all alone in Chicago - imperative that someone call her brother in law.

Earle Moyer
Camp Hill, Pa. (1802 Walnut St.)
and first her physician
Dr. Harold G. Wedell
(See attached names)

Apart from her social security benefits she is penniless - I believe she has a well to do brother. Do not know his name. Get it from Earle Moyer in hopes that he can provide for her -

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I owe Grant V. W. Roth, Pres. of Ace Foundry $10,000 - secured by a $10M life insurance policy, (in his possession) and all of my 1st Co.'s common stock, purpose of loan (now about 3rd year old) and explanation given: untrue -

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Schedule of insurance policies and loans in file, located in center drawer of my office desk - Beneficiary - not that it matters - Mrs. Nay, annuity for her life -

all entries (deposits) in my check books (generally in pencil) marked "loans" are all of them spurious, escrow and similar items - except 1.) real loans from Continental Bank, Consolidated Finance Co., First Securities Co. and Mrs. Nay (see statement prepared of amounts borrowed from her and repaid in my brief case) for last year and check stubs for 1968.-

She knew nothing of what I have been doing for years and was victimized more than anyone else - This to be borne in mind in case she survives, which I pray, that she will not. -

I phoned my brother George today (5/31) in Boston and asked - and obtained - his resignation as Executor of my will - He promised to confirm it in a letter dated today to be sent to the office.

June 1, 1968. - I had no accomplices and no help in these thefts. -

/s/ Leston B. Nay

RECEIVER'S EXHIBIT 13

RECEIVER'S EX. 13

NAME ARNOLD C SCHUERER
ADDRESS 740 N. FRANKLIN ST CHICAGO, ILL.

FIRST SECURITIES COMPANY OF CHICAGO

MAY

DATE	QUANTITY	SOLD	DESCRIPTION	PRICE	DEBIT	CREDIT	BALANCE	PROOF
	2000		MISSOURI KANSAS TEX ED 5/67	101 1/2	2045 74		267 74	
11	100		BACKSTAY BELT COM	RECD				
14		2000	MO KAN TEX ED 5/67	SOLD				
17			CHECK			267 74	00	267 74
AUG 5		50 RTS	AMERICAN HOUSE PRODS	1 5/16		43 14	CR 43 14	
	40 R		AMERICAN HOUSE PRODS COM	RECD				
NOV 16			CHECK		43 14		00	43

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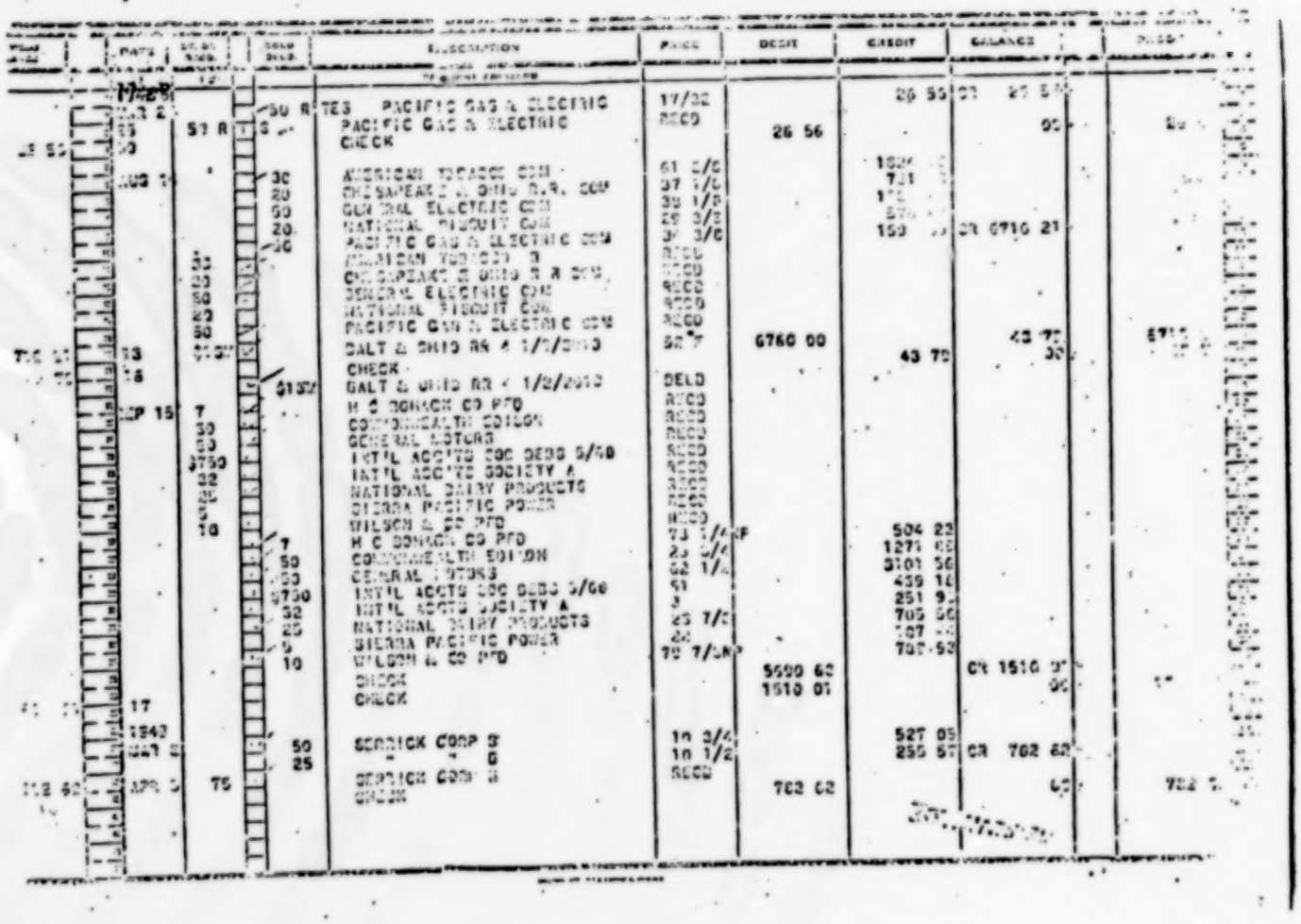
X R - 13

RECEIVER'S EXHIBIT NO. 13

MAY

DATE	QUANTITY	SOLD	DESCRIPTION	PRICE	DEBIT	CREDIT	BALANCE	PROOF
JUN 11	A/C 9	50 R	TSFR PACIFIC GAS & ELECTRIC	15/16		43 48	CR 43 48	
12	SOLD TO		PACIFIC GAS & ELECTRIC	RECD				
13			CHECK		43 48		00	43
SEP 29		5	NO IND PUB SVC	107 3/4		533 45		
		24	AMERICAN SMELTING & REF	99 3/8		1475 62		
		36	MARSHALL FIELD	27		1013 37		
		30	GENERAL MOTORS	57 5/8		1720 45		
		25	STD OIL OF INDIANA	38 7/8		965 91		
		38	SWIFT & CO	33 3/8		1255 70		
		10	AMERICAN TEL & TEL	157 5/8		1572 11		
		12	CHES & OHIO COM	44 5/8		531 62		
		60	AMERICAN RAD & STD SANITARY	13 3/8		798 32	CR 9573 07	
	35		MARSHALL FIELD & CO	RECD				
	24		AMERICAN SMELTING & REF	RECD				
	50		AMERICAN RAD & STD SANITARY	RECD				
	30		GENERAL MOTORS CORP COM	RECD				
	33		SWIFT & CO COM	RECD				
	10		AMERICAN TEL & TEL COM	RECD				
	12		CHES & OHIO R.R. COM	RECD				
	25		STD OIL CO OF INDIANA COM	RECD				
	6		NO IND PUB SVC CO CUM PFD	RECD				
30			NEW YORK & FED TAX A/C VARIOUS	TSFRS	9 18		CR 9564 49	9573 67
	10		AMERICAN TEL & TEL [EXL TD]	157 5/8	1572 11			
		10	AMERICAN TEL & TEL	157 3/8		1569 61	CR 9561 20	9564
OCT 1			SVC CHG VARIOUS TSFRS		50 00		CR 9611 95	9561
7			10/14/47 DIV 5 NO IND PUB SVC PFD		6 25		CR 9605 70	9511
24			CHECK		9597 90			
			TSFR TO A/C GORDON M VAUGHAN					
			IN ACCORDANCE WITH RESOLUTION					
			OF DISTRIBUTION OF VAUGHAN CO		7 84		00	7 84
27			TO RECORD CHECK #389 ISSUED					
			10/16/44 WHICH WAS MUTILATED			48 14	CR 48 14	
28			TO REPLACE CHECK MUTILATED		48 14		00	48


DESCRIPTION
PRICE
DEBIT
CREDIT
BALANCE
TES PACIFIC GAS & ELECTRIC
PACIFIC GAS & ELECTRIC
CHECK
26 56
CHECK
CHECK
CHECK

RECEIVER'S EXHIBIT 14

RECEIVER'S EXHIBIT 14

Name Eleanor A. Schuerer — Trust Securities Company
Address 1120 Lake Shore Dr — of Chicago.

CHICAGO ILL

DATE	ST. OF REG.	GOLD DELIV.	DESCRIPTION	PRICE	DEBIT	CREDIT	BALANCE
			AMOUNT FORWARD				
FEB 4		50	RTS CONSOL BISCUIT CO	3 1/8		151 19	CR 151 19
9	50		CONSOL BISCUIT RTS TO CENCEL TRADE 2/4/46	3 1/8	151 19		00
APR 15	1.2		GENERAL PUBL SV UTIL COM	23	28 60		28 60
20	1M		ASSOC GAS & ELEC 3 3/4 78 CHECK REC'D	RECD		28 60	00
22							
24		1M	ASSOC GAS & ELEC 3 3/4/78	DELD			
31			GENERAL PUBL UTIL	RECD			
		1.2	GENERAL PUBL UTIL	DELD			
APR 30	LONG 31		GENERAL PUBL UTIL				
SEP 3	LONG 31		GENERAL PUBLIC UTIL				
OCT 28		31	GENERAL PUBLIC UTIL COM	DELD			

FORWARDED

RECEIVER'S EXHIBIT NO. 14

DATE	ST. OF REG.	GOLD DELIV.	DESCRIPTION	PRICE	DEBIT	CREDIT	BALANCE
			AMOUNT FORWARD				
JAN 9	$2M		MISSOURI KANSAS TEXAS R.R.5/67	77 1/4	1555 50		1555 50
13			CHECK			1555 50	00
16		3	SOUTH CAROLINA ELEC & GAS COM	7 7/8		21 79	
		10	SO CAROLINA ELEC & GAS COM	7		70	22 40
17	3 10	000	SO CAROLINA ELEC & GAS COM	RECD			
FEB 4		$2000	MO KANSAS TEXAS R.R. 5/67	DELD			
SEP 17			CHECK		22 49		00
1948							
FEB 2	$1M		DENVER RIO GRAND & WEST R.R. INC "A" 4 1/2/2018	56 1/4	565 00		
	$1M		CHGO MILW ST PAUL & PAC "D" 4 1/2/2044	54 3/4	550 00		
	$1M		CHGO INDIANAPOLIS & LOUISVILLE RY INC A"A 4 1/2/2033	44 1/4	445 00		
	$1M		BALT & OHIO R.R. 4 1/2/2010	49 F	492 50		2052 50
MAR 1			CHECK			2052 50	00
		$1M	CHGO MILW ST PAUL & PAC B 4 1/2/2044 [CXL TO 2/27/48]	54 3/4		550 00	
A/O 2/27	$1M		CHGO MILW ST PAUL & PAC B 4 1/2/2044	54 3/4 PLUS INT	891 50		41 50
10			CHECK			41 50	00
25		$1M	BALT & OHIO R.R. 4 1/2/2010	DELD			
		$1M	CHGO IND.& LOUISVILLE 4 1/2/2	33 DELD			
		$1M	CHGO MILW ST PAUL 4 1/2/2044	DELD			
		$1M	DENVER R IO GRANDE & WEST 4 1/2/ 2018 A	DELD			
1949							
MAY 6	$2M		MO-KAN-TEX ADJ INC 5/57	70 F	1400 00		1400 00
			CHECK			1400 00	00
JUN 1		$2M	MO-KAN-TEX ADJ INC 5/57	DELD			

DATE	SOLD DELD.	DESCRIPTION	PRICE	DEBIT	CREDIT	BALANCE
1956						
19	50	CARR CONSOLIDATED BISCUIT			131 06	CR 131 06
	50	CARR CONSOLIDATED BISCUIT.				
		CHECK		131 06		00

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Montgomery St. Schweser Proj. Montana

DATE	SOLD DELD.	DESCRIPTION	PRICE	DEBIT	CREDIT	BALANCE
OCT15	31	GENERAL PUBLIC UTILITIES	RECD			
25	31	GENERAL PUBLIC UTILITIES	DELD			
1955						
OCT8	50	PATINO MINES " ENTERPRISES	5	256 40		256 40
14		CHECK			256 40	00
26	50	PATINO MINES ENTERPRISES	DELD			
1955						
JUL20	$1M	BOSTON-MAINE INCOME 4 1/2-7/1/70	56 3/4 F	567 50		
	$1M	NEW YORK NEW HAVE & HARTFORD RR CONV INC 4 1/2% 7/1/2022	55 F	550 00		
27		CHECK			1117 50	00
AUG22	$2M	N Y N HAVEN-HARTFORD 4 1/2	DELD			
	$1M	BOSTON MAINE INC A 4 1/2	DELD			
1957						
FEB11	$1M	BOSTON & MAINE RR 4 1/2-1970	58 F	582 50		
	$4M	BOSTON & MAINE RR 4 1/2-1970	58 F	2331 36		
		CHECK			2911 86	00
MAR11	$1M	BOSTON & MAINE RR 4 1/2-1970	DELD			
	$4M	BOSTON & MAINE RR 4 1/2-1970	DELD			
MAY13		INT-N Y N H & HARTFORD RY			27 50	CR 27 50
JUL22		DIV-PATINO MINES			25 00	52 50
AUG1		CHECK		52 50		00
SEP9	50	SWIFT & CO	31 3/4	1587 16		1587 16
16		CHECK			1617 16	00
23	50	SWIFT & CO	DELD			
1958						
MAR12	63	BOSTON & MAINE RR 4 1/2-7/1/70	16 3/4 F	1021 50		
	13	N Y, NEW HAVEN & HARTFORD RR 4 1/2- 1/1/2022	7 1/2F	76 50		
19		CHECK			1098 00	00
APR16	63	BOSTON & MAINE RR 4 1/2-7/1/70	17 1/2 F		1030 47	00
	13	NEW YORK, NEW HAVEN & HARTFORD RR 4 1/2- 1/1/2022	7 F		67 53	CR 1098 00
24		CHECK		1098 40		00

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OGREN EXHIBIT 9

OGREN EX. 9

PREPARED Jmh 12/6/67

APPROVED

First Securities Company of Chicago
10-31-67
Comments re significant matters

As of October 31, 1967, the Company did not meet the minimum capital requirements of the Midwest Stock Exchange by approximately $7,000. The Company was aware of this deficiency and corrected it in Nov. 1967.

On Dec. 6, 1967, I called Mr. Frank Rothing, V/P and Treas. of the Midwest Stock Exchange (who was aware of the deficiency and that it had been corrected). Mr. Rothing said that the Exchange did not believe that disclosure of the deficiency in the questionnaire was appropriate since it had been corrected. We agreed. Mr. Rothing said that if a Company had a deficiency which was not corrected within a reasonable time, the Exchange would suspend the Company for trading.

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